Supreme Court, U.S.
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No. _____

In The
Supreme Court of The United States
October Term 1997

JOHN A. COCHRANE,
Petitioner.

v.

TUDOR OAKS LIMITED PARTNERSHIP,
Respondent.

Petition For A Writ Of Certiorari To The United States Court of Appeals For The Eighth Circuit

PETITION FOR WRIT OF CERTIORARI

JOHN A. COCHRANE
Attorney at Law
24 East Fourth Street
St. Paul, MN 55101
(612) 298-1950

Attorney for Petitioner
Counsel of Record

APPELLATE ADVANTAGE
3723 N. OAK TRAFFICWAY◆KANSAS CITY, MO 64116◆816-453-2424

192 pp.

QUESTIONS PRESENTED

1. Whether a "breach of fiduciary duty" that resulted in no actual damage to a judgment creditor is a "defalcation" within the meaning of 11 U.S.C. § 523(a)(4),(1978) of the Bankruptcy Code.

2. Whether a "liquidating trustee" acting without actual and implied authority has standing to maintain claims based on a state court judgment in Bankruptcy Court on behalf of a non-existent Canadian limited partnership?

3. Whether the bankruptcy court may apply principles of full faith and credit under 28 U.S.C. § 1738, to a state court judgment when the issue of fraud was not litigated in state court and where the state court of appeals held that there was a genuine issue of material fact as to whether the judgment was obtained by fraud?

4. Whether a full and fair opportunity was afforded debtor to litigate lack of standing issues meets the requirements of 28 U.S.C. § 1738, where summary judgment was issued solely on the basis of collateral estoppel of state court judgment.

PARTIES TO THE PROCEEDINGS

Parties to the proceedings are Tudor Oaks Limited Partnership an Ontario Limited Partnership, plaintiff below, S.B. McLaughlin & Co., Ltd., a Canadian Corporation [as putative liquidating trustee of Tudor Oaks Condominium Project] and John A. Cochrane, Debtor.

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PETITION FOR A WRIT OF CERTIORARI

John Alexander Cochrane respectfully petitions for a writ of certiorari to review the opinion of the United States Court of Appeals for the Eighth Circuit in this case.

OPINIONS BELOW

The Opinion of the Eighth Circuit Court of Appeals found in Appendix A, Apdx. 1.

The Opinion of the U.S. District Court below is found in Appendix B, Apdx. 18.

The Opinion and Order of the Bankruptcy Court below is found in Appendix B, Apdx. 20.

The Opinion Cochrane v. Tudor Oaks of the Minnesota Court of Appeals is found in the Appendix D, Apdx 60.

The Opinion S.B. MCLAUGHLIN & Co. Ltd., v. John A. Cochrane et al. of the Minnesota Court of Appeals is found in Appendix D, Apdx. 99.

The Opinion of the Minnesota District Court is found in Appendix D, Apdx. 82

JURISDICTION

The opinion of the Unites States Court of Appeals for the Eighth Circuit was filed on September 5, 1997. A Motion to stay the entry of the mandate pending application for Certiorari was filed on October 15, 1997. Petitioner invokes the jurisdiction of this court under 28 U.S.C. § 1254(1), and 28 U.S.C. § 2101(c). This petition is timely having been filed within 90 days of September 5, 1997. Petition to Stay the Mandate was denied, November 17, 1997.

STATUTES INVOLVED

The statutory provision at issue, 11 U.S.C. § 523(a)(4), is reprinted in the appendix to this petition (Appendix C, Apdx. 41).

The statutory provision at issue, 28 U.S.C.A. § 1738, is reprinted in the Appendix to this petition. (Appendix C, Apdx. 51).

STATEMENT OF THE CASE

The Bankruptcy Courts jurisdiction below was based upon 11 U.S.C. § 301, the appeal to District Court was under 28 U.S.C. § 158(a)(1), the appeal to the Eighth Circuit was under 28 U.S.C. § 1291. John A. Cochrane, a lawyer, Debtor filed a voluntary petition in the Middle District of Florida, Tampa Division, Case No. 92-16497-9P1 on December 23, 1993. Despite an order staying transfer pending appeal the case was erroneously transferred and on April 30, 1993, The Minnesota Bankruptcy Judge assumed the case without a transfer order to the Minnesota Bankruptcy Court. Involuntarily conversion to a case under Chapter 7 occurred on May 26, 1994. Tudor Oaks Limited Partnership [sic] (Tudor Oaks), Plaintiff commenced an action objecting to the discharge of its judgment, alleging that it was not dischargeable under 11 U.S.C. § 523(a)(4).

Tudor Oak's claim relates to a condominium project in Minnesota developed by Tudor Oaks Condominium Project, an Ontario Limited Partnership, (Tudor Oaks) in which ABIO Holdings, Inc. (Minnesota), a Minnesota Corporation, was the General Partner. Tudor Oaks was formed by S.B. McLaughlin & Co., Ltd., Central Precision Ltd. and ONIX Development Ltd. The principals of these entities were S. Bruce McLaughlin, S.B. McLaughlin & Co., Ltd.; J. D. Crashley, Central Precision Ltd.; and David Owen, ONIX Developments Ltd. Each limited corporate partner owned a one-third

interest in the limited partnership and a one third interest in the general partner, which held a nominal 3% interest in the partnership. The project was financed by First Bank and other secondary lenders. First Bank foreclosed its first mortgage in 1986, bidding in at $5.3 million dollars. Thereafter, First Bank offered for sale its Sheriff's Certificate for $ 1.5 Million Dollars[1]. At all times material Tudor Oaks was insolvent and subject OT millions of dollars of liens and judgments. It became a non-existent entity when it lost its Canadian charter in August of 1990 prior to the trial and judgment in this case. Debtor was not made aware of this fact until the matter arose in the Florida bankruptcy proceedings in December 1993.

First Bank initiated deficiency actions against Tudor Oaks the general and limited partners and the individuals for Three and One Half Million Dollars ($3,500,000.00). Two of the three limited partners, (Owens and Crashley), Tudor Oaks and A.B.I.O. retained John Cochrane [Debtor] to represent them for a $20,000.00 fee to defend the deficiency action.[2]

S.B. McLaughlin & Co., Ltd. (McLaughlin) at all material times was represented by Counsel and proceeded

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[1]The offer was made to all limited partners in writing and was offered for sale to the public. Appendix E. Apdx. 145.

[2]Cochrane interposed answers on behalf of ABIO (Minnesota) and Tudor Oaks Condominium Project, the individuals. Owens & Crashley and their corporations ONIX, Ltd. And Central Precision Ltd. The case was in the discovery phase at time the Bank made its offer to sell the Sheriff's Certificate to the Defendants in that case on November 17, 1986. Appendix E. Apdx. 145.

separately. First Bank offered the Sheriff's Certificate for sale at $1,500,000.00. It reserved the right to sell it to the public or to anyone it chose to. If the bank sold the certificate to anyone other than the limited partners then no release of the deficiency judgment action would be given to the individual partners. The transaction had to be completed by the close of business December 17, 1986. Appendix E, Apdx. 145.

At the time of the offer, no partner was willing to advance $1.5 million an insolvent Tudor Oaks. Those funds would immediately be subject to seizure by judgment creditors who's claimed debts were millions of dollars. However, McLaughlin could only buy the Certificate in its own name. McLaughlin or S.B. McLaughlin, did not make a written offer to purchase the Certificate. The Minnesota Court of Appeals Stated:

> Cochrane arranged for several investors, including himself, to purchase the Sheriff's Certificate for $1,200,000.00. He and his clients agreed that he would retain a 20% interest in the property as a fee for arranging the purchase. Sixty percent of the property was purchased by Appellant K.S.C.S. Properties, Inc. of which Cochrane was a one-quarter shareholder. Cochrane and each of his three partners contributed $300,000.00 (Three Hundred Thousand dollars) for the sale. The remaining 20% interest, which at one point was expected to be transferred to Tudor

Oaks[3], was alternatively put in the names of two of K.S.C.S.'s shareholders, Roland Stinski and Bill Keefer.

In 1987, S.B. McLaughlin & Co. (McLaughlin) brought an action against John Cochrane, K.S.C.S. Properties, Inc., Tudor Oaks Condominium Project and ABIO Holdings, Inc. McLaughlin proceeded as plaintiff individually and derivative capacity on behalf of [Tudor Oaks] and ABIO, alleging Cochrane and K.S.C.S. breached their fiduciary duties. When the action was commenced [in 1987], Tudor Oaks was a limited partnership chartered in Ontario, Canada. ABIO, Tudor Oaks general partner, was a Minnesota corporation. McLaughlin was a limited partner of Tudor Oaks... . On August 19, 1990, Tudor Oaks lost its limited partnership charter in Ontario .... . On October 11, 1991, ABIO was statutorily dissolved in Minnesota. On December 12, 1991, McLaughlin moved to amend its complaint to reflect its sole ownership of

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[3]It is to be noted here that the remaining 20% interest was initially proposed to go to the Owen-Crashley interests not to Tudor Oaks. Appendix E. Apdx. 142. The Minnesota Court of Appeals here was in error.

> Tudor Oaks and ABIO. The District Court granted McLaughlin's motion on January 10, 1992.[4]
>
> This eliminated McLaughlin's derivative action against Tudor Oaks and ABIO, and realigned Tudor Oaks and ABIO as plaintiffs proceeding in their own right against Cochrane and K.S.C.S. The parties did not inform the Court that Tudor Oaks had dissolved or that ABIO was no longer a legal entity. Cochrane v. Tudor Oaks Condominium Project, 529 N.W.2d 429, 431, (Minn.Crt.App.1995). Appendix D, Apdx. 60.

A jury trial in 1992 resulted in a judgment in favor of McLaughlin against Debtor in the amount of $792,000.00, in favor of Tudor Oaks and against Debtor in the amount of $1,628,000.00 and against K.S.C.S.[5] in the amount of $3,520,000.00. The judgment was reduced to $1.6 million dollars and S.B. McLaughlin Co. Ltd., was held not to have a cause of action against Debtor, ab initio as there existed no attorney Client or fiduciary relationship between McLaughlin

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[4]Tudor Oaks was by this time a non existent entity and S.B. McLaughlin had purchased the shell of Tudor Oaks Condominium Project in September, 1989. Tab. 16.

[5]K.S.C.S. is a Minnesota Corporation with principal shareholders of Keefer, Stinski, Cochrane and Sandberg.

and Debtor.

An action was brought by Debtor in to vacate the judgment on the grounds of fraud. The Summary Judgment on denying that relief was appealed by Debtor to the Minnesota Court of Appeals.

The Minnesota Court of Appeals affirmed the District Court's refusal to vacate the judgment on fraud grounds and affirmed the lower Court's Summary Judgment on the grounds that Debtor had waived the fraud defense. The Court of Appeals however stated:

> Tudor Oaks conceded that its limited partnership registration had expired and that ABIO, its general partner, was dissolved. Cochrane, 529 N.W.2d, p. 431-432.

> We would note that it is the entitlement to recovery, not the actual capacity to recover by enforcing the judgment, which is the issue here. Like the panel of this court which decided the previous appeal in this matter, we do not reach the issue of who will enforce the judgment or how it will be enforced.

Cochrane 529 N.W.2d, p. 436 and S.B. McLaughlin & Co., Ltd. v. Cochrane, Appendix D, Apdx 99.

In the first Appellate Court decision the Court of Appeals stated at Footnote 3:

> The record indicates that the Tudor Oaks claim is now pursued singularly by S.B. McLaughlin. In September, he had purchased the interest of all the partners in Tudor Oaks. Appellants have not asserted and we have not explored issues surrounding McLaughlin's acquisition of benefits of suit by purchasing the interests of his partners. In fact, nothing in this record satisfactorily reflects the persons entitled to benefit from the ultimate judgment in favor of Tudor Oaks.

S.B. McLaughlin & Co. Ltd. v. Cochrane, Cite

Debtors' Answer alleged (1) lack of legal existence of the partnership, lack of standing of it and S.B. McLaughlin or S. Bruce McLaughlin individually to pursue the claim in Bankruptcy Court. Debtor also claims McLaughlin could not acquire the cause of action sounding in legal "malpractice" (breach of lawyers duties) by purchase which resulted in the judgment. The Bankruptcy Court Order dated March 29, 1995 granted Summary Judgment and dismissed the timely raised standing issue in its footnote #17, (Appendix B, Apdx. 38), plus ignoring the fact that no successor trustee had ever qualified or tried to qualify in Canada or in any U.S. Court proceeding.

The U.S. District Court affirmed the decision of the

Bankruptcy Court.[6]

The Bankruptcy Court[7] granted Summary Judgment for Tudor Oaks holding as a matter of law that Debtor was estopped from challenging the State Court Judgment and that the Judgment was non-dischargeable pursuant to 11 U.S.C. § 523 (a)(4). Appendix B, Apdx. 20.

The Eighth Circuit affirmed the District Courts affirmance of the Bankruptcy Court in the opinion filed September 5, 1996. Appendix A, Apdx. 1. The Eighth Circuit Court held that Tudor Oaks former partner as "so called liquidating trustee" had standing to bring the action although the partnership was a non-existing entity. Further, Debtor was collaterally bound by the State Court judgment in the Minnesota Court of Appeals, holding that the unlitigated issue of fraud and non-existence of the Plaintiff, Tudor Oaks had been waived by debtor. Appendix D, Apdx. 60. 529 N.W.2d 429, 436 (Minn.Crt.App.1995).

The panel drew a distinction between the capacity to sue defense in the Bankruptcy Court and the unlitigated capacity to sue defense that was held to have been waived in the second State Court proceeding.

Although the Eighth Circuit Court noted the Minnesota Court of Appeals affirmed the Summary Judgement

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[6]The Honorable Michael J. Davies, U. S. District Judge, District of Minnesota. Appendix B, Apdx. 8.

[7]The Honorable Gregory F. Kishel, United States Bankruptcy Court for the District of Minnesota. Appendix B, Apdx. 20.

on the fraud issue in the Debtors' action solely upon the finding of waiver, the panel nevertheless went on the hold Debtor was, for the purpose of applying the doctrine of the collateral estoppel, estopped because the litigation had reached such a stage that in the panels view there is "no really good reason for reviewing [those issues] to be litigated again." The panel did not therein address the issues of a non-existent entity, Tudor Oaks, of obtaining the judgment or that the "liquidating trustee" was never party to the original litigation.

Here there was no trust, no funds, money or property held, taken, or denied to any client of the Debtor in these proceedings.

The panel was in error when it asserts that Cochrane failed to disclose to his clients[8] his interest in K.S.C.S. Inc. Present at the closing at the Bank on December 17, 1986 were the representative of the Bank, the Debtor, Crashley, Heath, Owen's lawyer, Owens, the share holders of K.S.C.S Inc. Stinski & Keefer, Sandberg, & Cochrane. At closing the Debtor read out loud in hac verba each and every document including the Articles of Incorporation of K.S.C.S. and its By-Laws and the final agreement making disclosure of ownership to all parties before the execution of any closing documents.

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[8]Debtors, clients were Tudor Oaks, Crashley, or A.B.I.O., Central Precision (Crashley) ONIX (Owens).

Owens, Crashley, & Heath[9] were present when the K.S.C.S. documents were read. and signed off on the purchase agreement which recites Debtor's interest in K.S.C.S.

The Eighth Circuit held that the question of "fiduciary duty" capacity is a federal question that "defalcation does not require evidence of intentional fraud or other intentional wrong doing. The panel then cited Lewis v. Scott, 97 F.3d, 1186 as the governing standard to be applied:

> Defalcation is defined as the "misappropriation of trust funds or money held in any fiduciary capacity; [the] failure to properly account for such funds." Under section 523(a)(4), defalcation "includes the innocent default of a fiduciary who fails to account fully for money received." . . . An individual may be liable for defalcation without having the intent to defraud.

The purchase documents signed by all of Debtors, Clients, the principals of K.S.C.S. and the Bank shows clearly the full disclosure of the Debtors interest in K.S.C.S. (Appendix E. Apdx 117) and the absence of any defalcation as defined in Lewis(Id.) or elsewhere in the law.

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[9]Owens, Heath and S.B. McLaughlin are Canadian Lawyers and Crashley is a sophisticated investor.

SUMMARY OF ARGUMENT
REASONS FOR GRANTING THE WRIT

I. THE EIGHTH CIRCUIT HOLDING CONFLICTS WITH DECISIONS OF OTHER UNITED STATES CIRCUIT COURTS CONTRARY TO EXISTING DECISIONS OF THE UNITED STATES SUPREME COURT.

It is plaintiff's burden to prove non-dischargeability by a preponderance of the evidence. Grogan v. Garner, 498 U.S. 279, 111 S.Ct. 654, 112, L.Ed. 755,(1991). Two elements must be present 1.) fraud or defalcation by the debtor, 2.) while he or she is acting as a fiduciary. There are two lines of cases that interpret this section, each focusing on a different word in § 523(a)(4). Those two theories when applied to this case leads to contrary results.

Beginning with the Supreme Court decision in Chapman v. Forsyth, 43 U.S. 202, 11 L.Ed. 236, (1844) and Davis V. Aetna Acceptance Co., 293 U.S. 328, 55 Sp.Ct. 151, 79 L.Ed. 393, (1934). Courts have held that the fiduciary relationship referred in § 523(a)(4) is limited to instances involving express and "technical" trusts.

Lower court decisions strictly defining a fiduciary as a trustee, couple it with a broad definition of "defalcation". A defalcation may be an innocent default "so as to include all fiduciaries who for any reason were short in their accounts" Central Hanover Bank & Trust Co., v. Herbst, 93 F.2d, 510

C.C.A. 2, (1937) interpreting 11 U.S.C. § 35(a)(4).

The trustee theory of § 523(a)(4) imposes potential liability on a debtor who must be a trustee under either an express or technical trust rather than a trustee under a imposed ex-maleficio trust. See In re Teichman, 774 F.2d, 1395 (9th Cir. 1985); In re Johnson, 691 F.2d, 249 (6th Cir. 1982); In re Pedrazzini, 644 F.2d, 756 (9th Cir.1981); Matter of Angelle, 610 F.2d, 1335 (5th Cir.1980); In re Romero, [*10] 535 F.2d 618 (10th Cir. 1976); Matter of Dloogoff, 600 F.2d, 166 (8th Cir.1979). The distinction, then between an express trust and a trust imposed ex-maleficio is that an express trust comes into existence prior to the act of wrongdoing from which the debt arose. A trust imposed ex-maleficio, on the other hand, springs into existence from the very act of wrongdoing and is applied constructively as a remedy for wrongdoing to prevent unjust enrichment. Hayton v. Eichelberger,In re Eichelberger), 100 Bankr, 861, 863-864 (Bankr. S.D.Tex. 1989). Accord, Morgan v. Musgrove (Matter of Musgrove), 187 Bankr. 808 (Bankr. N.D.Ga. 1995).

A "fiduciary" for § 523(a)(4) purposes is a person who controls an express, technical, or statutory trust, then loss of the entrusted funds or property by the fiduciary acting in a fiduciary capacity is a defalcation. "It is axiomatic that before there can be trust there must be a responsibility for particular property entrusted to the fiduciary for the benefit of another" In re Hamilton, 147 Bankr. 779, 793, (Bankr. D.Colo.1992), affirmed 46 F.3d, 1151, (10 Cir.1994)

The "newer" or broader line of cases narrowly defining "defalcation and broadly define fiduciary" is set out in Matter of Marchionido, 13 F.3d, 1111, (7th Cir.1994). The Court explained that a fiduciary relationship required the existence of a duty to another before the wrong occurred and defined § 523 (a)(4) fiduciary as one who:

> .... may know much more by reason of professional status, or the relation may be one that requires the principal to repose a special confidence in the fiduciary. Marcheanido, 13 F.3d, 1116.

However, the Sixth Circuit Court of Appeals and the Fifth Circuit Court of Appeals agree with a narrower definition of defalcation as a willful or reckless breach of a fiduciary duty. In re Johnson, 691 F.2d, 249, (6th Cir.1982). Matter of Moreno, 892 F.2d, 417, (5th Cir.1990). The Eleventh Circuit recognized the split of authority under § 523(a)(4) as to the definition of defalcation but did not resolve the split in the 11 Circuit as the actors conduct was clearly beyond negligent defalcation. Quaif v. Johnson, 4 F.4d, 955.

The only two cases in which there were no trust funds or other Trust assets which were lost are the instant case and Horsch v. Eisenberg (In re Eisenberg) 189 Bankr. 731 (Bankr. E.D.Wis.1995). It is to be remembered that the Bank owned the Sheriff's Certificate. Tudor Oaks owned nothing. The Bank could have donated the Certificate to charity if it had chose to do so.

Under the Eighth Circuit's view of the "defalcation"

theory under § 523 (a)(4) any professional breach of duty of whatever nature whether that resulting in a loss or not, would render the debt of a state court judgment non-dischargeable. The "trustee" theory of the law is founded in over 100 years of jurisprudence and was known to the Congress when it enacted the Bankruptcy Code in 1978.

The broad sweep of the instant opinion is at odds with the long standing interpretational rule of the Eighth Circuit Court of Appeals, that exemptions from discharge are to be strictly construed so as to give maximum effect to the policy of bankruptcy to provide debtors with a "fresh start". See e.g. In re Klein, 65 F.3d 749, 751, (8th Cir.1995) and Werner v. Hoffman, 5 F.3d 1170, 1172, (8th Cir.1993) (per Curiam)

> The proper application of § 523(a)(4) to implement the congressional policy of a "fresh start" requires that a conservative approach be adhered to so as not to erode that policy.

The Sixth Circuit Court of Appeals recently addressed the question of non-dischargeability of a Claim against a lawyer. Garner v. R.E. America, Inc., 1997 Fed. App. 0182(P) (6th Cir.) 1997 U.S. App. Lexus 14653, (1997).

As here it was undisputed that no embezzlement or larceny occurred in the case and there was no allegation or finding of fraud on the part of the Debtor. In Garner, reversing the lower Court the Sixth Circuit in its review of the case law found that the courts generally require; 1.) a fiduciary relationship; 2.) a breach of fiduciary relationship; 3.) resulting

loss [damage], but differ as to the nature of the fiduciary relationship necessary to trigger the defalcation provision of § 523(a)(4).

As pointed out in footnote (6) of Garner id., the dictionary definition of Black Law Dictionary, 6th Edition, expands the concept of defalcation to a untenable level:

> Because the attorney/client relationship by itself is insufficient to create the necessary fiduciary relationship for purpose of the defalcation provisions of § 523(a)(4), an attorney breach of fiduciary duty, without more does not constitute defalcation absent an express of technical trust, on attorneys legal malpractice, like all other types of professional legal practice remains dischargeable under the Code. Freeman v. Frick, 201 Bankr. 731, 738 (Bankr. N.D. Fla, 1997) "to extend the scope of § 523(a)(4) generally to acts of malpractice or unethical conduct of professionals goes well beyond the legal standing precedents of Courts in this Circuit or the U.S. Supreme Court."
>
> While attorneys should perhaps be held to a higher standard than other professionals, that is a decision for Congress, not the Federal Courts to make." Garner id. N. 6.

PLAINTIFF LACKS STANDING TO PRESS THE JUDGMENT CLAIM

II. THE COURT ERRED BY HOLDING THAT PLAINTIFF HAS STANDING TO MAINTAIN AN

ACTION UNDER 11 U.S.C. § 523.

Debtor, in his answer to the plaintiff's complaint affirmatively alleged the lack of existence of the partnership and the lack of standing of McLaughlin or S. Bruce McLaughlin individually a precursor of jurisdiction to pursue this claim.[10]

The Ontario Limited Partnerships Act 6 RSO, Ch. L. 16, § 21 (1990) provides that the dissolution of a corporate general partner automatically dissolves a limited partnership unless the partnership is continued by the **remaining general partners** pursuant to the partnership agreement or by consent. Tudor Oaks had only one general partner, the dissolved corporation ABIO, and it is undisputed that the partnership agreement did not contain any provision or continuation.

Defendant's answer raised the issue of standing, the validity of the judgment, and the capacity to sue in paragraphs 2, 4, 5, 15, 25, 26, 27, 28 and 29. A timely challenge was asserted in the Bankruptcy Court. Capital Fire Insurance Co. of California v. Langhorne, 146 F.2d 237, 243, (8th Cir.1945). The issue of standing was dismissed in footnote 17, Add. p. 14. Ontario law provides that a limited partnership

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[10]Debtor also raised the issue in the Minnesota proceedings that McLaughlin could not acquire "the cause of action sounding in "malpractice" by purchase. Minnesota Court of Appeals has recently affirmed this doctrine in Appletree Square A Limited Partnership and Business Consultants, Inc. As Liquidating Partnership and Business Consultants, Inc. V. O'Connor & Hamman. Cite (1997)

automatically dissolves upon the dissolution of its corporate general partner unless continued by (1) the remaining general partners pursuant to the partnership agreement or (2) by consent. Here there were no existing non-corporate general partners. There was only the dissolved corporate general partner that was dissolved by operation of Minnesota law and a dissolved limited partnership, but no remaining general partner. Likewise, there was no consent, nor could there be since under Ontario law the partnership itself had ceased to exist in 1990.

Accordingly, we have a final judgment in favor of a non-existent entity which commenced a non-dischargability action in Bankruptcy Court, in the name of a non-existent entity, Tudor Oaks Partnership, [sic]. The Minnesota Court of Appeals in two separate instances could not determine who could or should pursue the claim of the judgment. However, the Bankruptcy Court dismissed this lack of standing as not "deserve[ing] extended discussion". (Appendix B, Apdx. 20). Despite the acknowledgment by all parties and the Minnesota Court of Appeals that there is no such entity as Tudor Oaks nor was there one at the time of trial, this law suit refused to die. Unless reversed the perverse result will be that McLaughlin, who was not represented by Debtor, who the Minnesota Court of Appeals found did not have a fiduciary relationship with Debtor, who was not Debtor's client, who did not have a cause of action against Debtor, will make a recovery through a "phantom" entity that ceased to exist one and one half years before the trial of the merits of matter and

was a "shell" entity when McLaughlin purchased it in 1989 in order to pursue the action.

A clearer exposition for reversal is contained in Judge Foley's dissent in Cochrane v. Tudor Oaks Condominium Project., 529 N.W.2d 429, 436, (Minn.Crt.App.1995).

> "Therefore, at the time of the realignment of the parties in January 1992, Tudor Oaks was a nonexistent limited partnership, a nonentity. As I view the record, no one seriously disputes the fact that Tudor Oaks is a phantom judgment creditor, now, and when judgment was entered in its favor."
>
> Although capacity ordinarily should be raised by specifically negative averment, capacity to sue was not an issue at the time of the original complaint,[11] Tudor Oaks and ABIO were defendants, rather than plaintiffs. Further-more at the time neither Tudor Oaks nor ABIO had been dissolved. Once they were dissolved, they ceased to exist as legal entities. Cochrane, 529 N.W. 2d, 437. And further, the cases cited by the majority are distinguishable, since they involve entities or individuals that actually exist. Here, it is conceded that when judgment was entered in its favor:
>
> Tudor Oaks was a nonexistent entity, the possibility of enforcement of the judgment is equally nonexistent, and the judgment should be discharged of record. The judgment

---

[11]The action was commenced in June, 1987.

> in favor of Tudor Oaks is a void judgment and "cannot gain validity by the passage of time." (citation omitted) See footnote 1.

Cochrane, 529 N.W.2d. 438.

The legal question of the right of a non-existing entity to make and proceed with a bankruptcy claim in a U.S. Bankruptcy Court was addressed in Nebraska Mercantile Co. v. Nathanson Brothers. Co., 20 F.2d, 330 (8th Cir.1927) where in an analogous situation the court held at p. 332:

> As the corporation was dissolved and dead before the claim was filed or presented by its former treasurer for the corporation, it is clear the corporation as such did not and could not have a claim to present. Therefore the claim as originally presented could not be allowed. While, under the laws of the Nebraska, directors of a corporation at its dissolution by operation of law became trustees of its property for the benefit of shareholders, yet the directors became trustees only of property owned by the corporation at the time of its dissolution. [emphasis added] In this case, by assignment made on authority of a resolution of the board of directors of the Mercantile Company, all of its property, including the claim in question, had passed to a trustee for the benefit of its shareholders under an express trust. Who, then, in such case, was authorized to make the claim or have it allowed, save such trustee, to whom the claim had been duly transferred by assignment? While such objection is not

made or stressed by the objections filed, yet it arises plainly on the face of the record, and is open to inquiry on the question of the proper filing and proof of the claim. (emphasis added)

Here, McLaughlin acquired all of Tudor Oaks by purchase and thus was the sole corporate limited partner in September, 1989.

Neither McLaughlin nor its counsel notified Debtor or the Court of the September 1989 purchase in Canada until trial was imminent in 1991.

After the re-alignment of the parties in December 1991 making the non-existent entity, Tudor Oaks a co-party, plaintiff, the only "real" plaintiff was McLaughlin, who the Minnesota Court held did not have a cause of action against Debtor.

As a matter of Federal Bankruptcy law, what efficacy does a state court judgment have where the record clearly shows that there is an issue of material fact that the judgment against the Debtor may have been obtained by fraud? Appendix D, Apdx. 82.

Title 28, U.S.C.A. § 1738 affords a challenge to state court judgments.

In this case, " The Bankruptcy Court held"... . The Plaintiff (Tudor Oaks), relies entirely on the doctrine of Collateral Estoppel, or "issue preclusion". Appendix C, Apdx. 51. Where proceedings below at the trial level and through judgment review are legally deficient and fundamentally flawed they should be denied recognition under 28, U.S.C.

1738. In Kremer v. Chemical Construction Corp., 456 U.S. 461, 480, (1982) the Supreme Court said:

> ...we have previously recognized that judicially created doctrine of collateral estoppel does not apply when the party against whom the earlier decision is asserted did not have a full and fair opportunity to litigate the claim of issue."

The Kremer Court held that "redetermination of issues is warranted if there is reason to doubt the quality, extensiveness or fairness of procedures in prior litigation" citing Montana v. United States, 440 U.S. 147, (1979).

Here it is not denied that the claim was prosecuted by McLaughlin who pressed the litigation, paid the lawyers and is pressing the claims under the aegis of Tudor Oaks.[12]

As was held in Montana, 440 U.S., 223, n. 11:

> "Redetermination of issues is warranted if there is reason to doubt the quality, extensiveness, or fairness of procedures followed in prior litigation." (Citations omitted)

In Heiser v. Woodruff, 327 U.S. 724, 736, (1985) the Supreme Court said at p. 737:

---

[12]ONIX Developments, Central Precision, Owens and Crashley were completely satisfied with Debtor's representation and so testified at trial as Debtor had obtained releases for them and their corporate entities in the deficiency judgment actions to the tune of 3.5 Million Dollars.

> Undoubtedly, since the bankruptcy act authorizes a proof of claim based on a judgment, such a proof may be assailed in the bankruptcy court on the ground that the purported judgment is not a judgment because of want of jurisdiction of the court which rendered it over the persons of the parties or the subject matter of the suit, or because it was procured by fraud of a party. (emphasis added)

Non-dischargeability proceedings are to be decided by Federal Bankruptcy Courts because they deal with very special federal interests. Justice Blackmun said:

> "Because res judicata may govern grounds and defenses not previously litigated, however, it blockades unexplored paths that may lead to truth. For the sake of repose, res judicata shields the fraud and the cheat as well as the honest person. It therefore is to be invoked only after careful inquiry. Petitioner contends, and we agree, that here careful inquiry reveals that neither the interests served by res judicata, the process of orderly adjudication in state courts, nor the policies of the Bankruptcy Act would be well served by foreclosing petitioner from submitting additional evidence to prove his case." (emphasis supplied)
> Brown v. Felsen, 442 U.S., 127,132, (1979)

At review of the issue of collateral estoppel and res adjudicata in, In re Kurtz, 170 Bankr. 596, (E.D. Mich.1994), states: "Actually litigated means something more than a mere opportunity to litigate."

In its review of the Bankruptcy Court's need to grant full faith and credit to a State Court judgment, the Court showed the great weight of authority holds that:

> If impartial issues were not actually litigated in the prior proceeding as in the case of a default judgment then, collateral estoppel does not bar re-litigation in the Bankruptcy Court.

Quoting Spillman v. Harley, 656 F.2d, 228.

Here it is undisputed that the issue of fraud & standing in obtaining the judgment and pursuing it in Bankruptcy Court was never "actually litigated." The words "actually litigated" taken on their plain meaning cannot reasonably be construed to mean a "mere opportunity to litigate". Kurtz Supra.

The question whether Debtor committed "fraud or defalcation" while acting in a fiduciary capacity under 11 U.S.C. § 523(a)(4) was neither actually litigated nor was it essential to that state court proceeding.

Here no objective observer can say that a judgment obtained following an impermissive purchase of a cause of action, resulting in a judgment obtained in the name of a non-existent "phantom" entity for over a million dollars, should be afforded full faith and credit, under 28 U.S.C.A. § 1738, where there exists an

issue of material fact as to whether the judgment was obtained by fraud and the cause of action was a "purchased malpractice" action. The after acquired rights afforded to a debtor under Title 11 of the U.S. Bankruptcy Code and Rules cannot be usurped through the mechanism of such an infirm state court judgment.

The Eighth Circuit Bankruptcy Court's flawed analysis holds that Plaintiff action constitutes a partners exercise of rights "necessary to wind up the affairs of the partnership to complete transactions begun but unfinished at the time of dissolution. Here at the time of dissolution of Tudor Oaks it had no cause of action against the debtor: For the foregoing reasons the Writ should issue.

EVEN IF DEBTOR COMMITTED A "DEFALCATION" WITHIN THE MEANING OF 11 U.S.C. § 523(a)(4) DEBTOR DID NOT CAUSE ANY DAMAGE TO PLAINTIFF

The Bankruptcy Court here and the Eighth Circuit Court of Appeals, would create an absolute, nondischargeable liability without any clear Congressional intent to impose such liability. Is conceded there was no express trust, and no funds were held by debtor, so upon what obligations or trust did the debtor "defalcate" to produce loss? Not a "corporate" opportunity since the plaintiff was insolvent, owned nothing and incapable of pursuing any opportunity is such ever existed and the "corporate" opportunity claim was abandoned at the trial court level. Here the holdings are clearly erroneous.

CONCLUSION

By impermissibly relying strictly on the doctrine of collateral estoppel, the Bankruptcy Court and the Circuit Court has allowed the non-dischargeability under 11 U.S.C.A. §523(a)(4) to be defined in a state court action, without regard to whether a "defalcation" has in fact, occurred.

As McLaughlin, Canadian lawyer, so aptly testified at trial: "Well when you have a sinking partnership, if you put more money, fresh money it goes down the drain, you are correct."

As there was no damage to Tudor Oaks, Debtors acts could not be defalcation under U.S.C. § 523 (a)(4).

For all the foregoing reasons the Writ should issue.

December 4, 1997.

Respectfully Submitted,

John A. Cochrane
Debtor
MN. Atty I.D. No.17577
Admitted to Sup. Court
Bar on October 1, 1963.
24 East 4th St.
St. Paul, MN 55101
(612) 298-1950
Fax (612) 298-0089

Of Counsel:

Loper & Seymour, P.A.
Stewart C. Loper
MN ATTY I.D.# 64476
24 East 4th St.
Suite 201
St. Paul, MN 55101
(612) 291-2954

APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

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United States Court of Appeals
FOR THE EIGHTH CIRCUIT

No. 96-1544

In re: John A. Cochrane, Debtor.	*	
----------	*	
Tudor Oaks Limited Partnership, Appellee,	*	Appeal from the United States District Court for the District of Minnesota
v.	*	
John Alexander Cochrane, Appellant.	*	

Submitted: December 11, 1996

Filed: September 5, 1997

Before McMILLIAN, JOHN R. GIBSON and MAGILL, Circuit Judges.

McMILLIAN, Circuit Judge.

John A. Cochrane, a Minnesota attorney and Chapter 7 debtor in bankruptcy, appeals from a final order entered in the United States District Court[1] for the District of Minnesota affirming a decision of the United States Bankruptcy Court[2] for the District of Minnesota (hereinafter the bankruptcy court) granting summary judgment in favor of Tudor Oaks Limited Partnership (Tudor Oaks) and holding as a matter of law that Cochrane's debt to Tudor Oaks, which has been reduced to a final state court judgment, is nondischargeable in bankruptcy pursuant to 11 U.S.C. § 523(a)(4). Tudor Oaks Ltd. Partnership v. Cochrane (In re Cochrane), Civ. No. 3-95-389 (D. Minn. Feb. 6, 1996), aff'g 179 B.R. 628 (Bankr. D. Minn. 1995). For reversal, Cochrane argues that the bankruptcy court erred in holding that (1) Tudor Oaks had standing to bring the present adversary proceeding in bankruptcy court, (2) Cochrane is collaterally estopped from relitigating factual findings upon which the underlying state court judgment was based, and (3) 11 U.S.C. § 523(a)(4) applies as a matter of law to bar discharge of Cochrane's judgment debt to Tudor Oaks. For the reasons discussed below, we affirm.

---

[1]The Honorable Michael J. Davis, United States District Judge for the District of Minnesota.

[2]The Honorable Gregory F. Kishel, United States Bankruptcy Judge for the District of Minnesota.

Background

The judgment debt that is the subject of this litigation arose out of a Minnesota state court action (hereinafter referred to as "the underlying state court action") which was filed in 1987 by S.B. McLaughlin & Co. (McLaughlin), a former Tudor Oaks partner. McLaughlin originally sued Cochrane, Tudor Oaks, K.S.C.S. Properties, Inc. (KSCS), and others in Minnesota state court on a theory of breach of fiduciary duties. At the time the action was commenced, Tudor Oaks was a limited partnership chartered in Ontario, Canada. The parties were subsequently realigned, and Tudor Oaks became a plaintiff while Cochrane and KSCS remained defendants. The case proceeded to trial before a jury in the summer of 1992. By that time, Tudor Oaks had dissolved, but the state trial court was not informed of the dissolution. At trial, the jury rendered a special verdict which found, among other things, that Cochrane had breached a fiduciary duty to Tudor Oaks resulting in damages of $1.628 million and that Cochrane and KSCS had conspired to breach fiduciary duties to Tudor Oaks resulting in damages of $3.52 million. The state trial court entered judgment against Cochrane awarding Tudor Oaks $1.628 million plus prejudgment interest and further entered judgment against KSCS awarding Tudor Oaks $3.52 million plus prejudgment interest. On appeal, the Minnesota Court of Appeals, among other things, affirmed the finding that Cochrane had breached

his fiduciary duties, ordered a reduction in the total amount of damages awarded to Tudor Oaks from Cochrane and KSCS, and remanded the case to the state trial court with directions.[3] Accordingly, the state trial court, on remand, entered final judgment holding Cochrane and KSCS jointly and severally liable to Tudor Oaks in the amount of $1,722,025.52.[4] S.B. McLaughlin & Co. v. Cochrane, No. 87-11035 (Minn. Dist. Ct. Apr. 11, 1994) (amended order).

Cochrane then brought a separate action in Minnesota state court (hereinafter referred to as "Cochrane's independent state court action") seeking to have Tudor Oaks's judgment against him and KSCS vacated on grounds that Tudor Oaks's dissolution during the pendency of the underlying state court action deprived the trial court of subject matter jurisdiction or that the judgment was obtained by fraud. The trial court in Cochrane's independent state court action entered summary judgment in favor of Tudor Oaks and dismissed Cochrane's claims. Cochrane v. Tudor Oaks Condominium Project, No. 93-16553 (Minn. Dist. Ct. July 6, 1994). The state trial court reasoned: Cochrane's failure to raise a capacity-to-sue defense during the underlying state court action resulted in a waiver, Id. at 9; the record failed as a

---

[3]The Minnesota Court of Appeals also reversed a judgment in favor of McLaughlin.

[4]The total award included $1,256,666.00 in damages, $465,359.52 in prejudgment interest, and $22,542.70 in costs and disbursements.

matter of law to establish that Tudor Oaks perpetrated a fraud on the trial court in the underlying state court action or that the judgment in the underlying state court action was obtained by fraud, Id. at 11- 12; and, finally, although Tudor Oaks did not have a right to maintain the action, McLaughlin had a right to continue the action commenced before Tudor Oaks's dissolution, Id. at 14-15. On March 28, 1995, the Minnesota Court of Appeals affirmed the dismissal of Cochrane's independent state court action. Id., 529 N.W.2d 429 (Minn. Ct. App. 1995). The Minnesota Court of Appeals held that, in light of the protracted nature of the underlying litigation and the fact that Tudor Oaks's dissolution had long been a matter of public record, Cochrane's failure to challenge Tudor Oaks's capacity to sue until after the entry of final judgment resulted in a waiver. Id. at 435-36.

In the meantime, in December 1992, Cochrane filed for Chapter 11 relief in bankruptcy in the United States Bankruptcy Court for the Middle District of Florida. Cochrane listed Tudor Oaks among his creditors on his Schedule F. The Florida bankruptcy court transferred the case to the District of Minnesota. The bankruptcy court in Minnesota granted Tudor Oaks's request for relief from the automatic stay under 11 U.S.C. § 362, thereby permitting the underlying state court action to proceed to final judgment. The bankruptcy court also converted Cochrane's Chapter 11 bankruptcy case to a Chapter 7 proceeding. On May 24, 1994, following the entry of final judgment in the underlying

state court action, Tudor Oaks -- by and through its former partner and so-called "liquidating trustee," McLaughlin -- brought the present adversary proceeding in Cochrane's bankruptcy case and moved for summary judgment, claiming that Cochrane's judgment debt to Tudor Oaks is nondischargeable by operation of 11 U.S.C. § 523(a)(4). Section 523(a)(4) provides: "A discharge [in bankruptcy] does not discharge an individual debtor from any debt . . . for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny." Upon review, the bankruptcy court considered final and binding certain factual findings made in the underlying state court action. In reciting "the pertinent facts that were settled by the Minnesota state courts' decisions," 179 B.R. at 631, the bankruptcy court noted the following. Cochrane had been engaged by Tudor Oaks and two of the three Tudor Oaks partners (other than McLaughlin), to represent them in a bank foreclosure on a multimillion dollar condominium real estate development project that had failed financially. He was to be paid a flat fee of $20,000.00. Id. Cochrane purported to assemble a group of investors, incorporated as KSCS, to purchase the failed project at the sheriff's sale. Cochrane led his clients to believe that a 20% interest in the project would be retained by Tudor Oaks, with the remainder going to KSCS (receiving 60%) and two individual KSCS shareholders (together receiving 20%). To the contrary, however, Cochrane kept for himself as a "fee" the 20% interest which his clients expected

to retain, and he also failed to disclose to his clients that he was a 25% shareholder in KSCS. Id. at 631-32. Moreover, the bankruptcy court noted, the jury found that Cochrane breached his fiduciary duties as a result of: (1) his personal participation in the purchase of the sheriff's certificate as a shareholder of KSCS; (2) his involvement in the transaction that defeated Tudor Oaks's expectation that it would retain the 20% interest in the real estate; and (3) his charge of what amounted to a 20% contingency fee. Id. at 632. In light of these facts, the bankruptcy court concluded that the judgment debt Cochrane owed to Tudor Oaks was "for fraud or defalcation while acting in a fiduciary capacity." Id. at 632-36. In reaching this conclusion, the bankruptcy court determined that the attorney-client relationship involves fiduciary duties and that the term "defalcation," as used in §523(a)(4), includes innocent and negligent as well as intentional wrongful acts. Id. at 634-35. The bankruptcy court thus held that there was no genuine issue of material fact and Tudor Oaks was entitled to judgment as a matter of law on its claim that Cochrane's judgment debt was nondischargeable by operation of 11 U.S.C. § 523(a)(4). Id. at 636. On appeal, the district court summarily affirmed. Cochrane appealed.

Discussion

We review the bankruptcy court's grant of summary judgment de novo. Our review is the same as that of the

district court. Summary judgment was properly granted if, assuming all reasonable inferences favorable to the non-moving party, there is no genuine issue as to any material fact and the moving party is entitled to judgment as a matter of law. Fed. R. Civ. P. 56(c); see, e.g., Celotex Corp. v. Cattrett, 477 U.S. 317, 322-23 (1986); Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 249-50 (1986); Get Away Club, Inc. v. Coleman, 969 F.2d 664, 666 (8th Cir. 1992); St. Paul Fire & Marine Ins. Co. v. FDIC, 968 F.2d 695, 699 (8th Cir. 1992). Where the unresolved issues are primarily legal rather than factual, summary judgment is particularly appropriate. Crain v. Board of Police Comm'rs, 920 F.2d 1402, 1405-06 (8th Cir. 1990).

Standing

Cochrane first argues that the bankruptcy court erred in failing to dismiss Tudor Oaks's adversary proceeding on the ground that Tudor Oaks, a dissolved partnership, lacked standing to bring this proceeding in bankruptcy court. As stated above, Tudor Oaks's former partner and so-called "liquidating trustee," McLaughlin, filed this adversary proceeding on behalf of Tudor Oaks. Nevertheless, Cochrane argues that, because Tudor Oaks was dissolved by operation of Ontario law (the law applicable to the partnership) prior to his bankruptcy filing, it is a non-existent entity and neither Tudor Oaks nor McLaughlin can engage in the present bankruptcy litigation.

In rejecting Cochrane's standing argument, the bankruptcy court explained as follows:

> [r]egardless of whether the named party-plaintiff [i.e., Tudor Oaks] is a valid, subsisting legal entity with capacity to sue or be sued, its one remaining partner has a right under Ontario law to wind up the affairs and to continue litigation under its name to do so. During the pendency of this adversary proceeding, the Hennepin County District Court held to that effect, in ruling against [Cochrane] in his independent lawsuit for relief from the original judgment in [Tudor Oaks's] favor. [Cochrane] is collaterally bound by this ruling, even though he apparently has an appeal from that judgment pending.

179 B.R. at 636 n.17 (citations omitted).

We first consider the bankruptcy court's collateral estoppel rationale with respect to the standing issue. The application of collateral estoppel is an issue of law which we review de novo. United States v. Brekke, 97 F.3d 1044, 1046-47 (8th Cir. 1996), cert. denied, 117 S. Ct. 1281 (1997). The bankruptcy court did not err in observing that collateral estoppel may apply to a trial court's ruling on the merits of an issue notwithstanding the pendency of an appeal from that

ruling.[5] See Morrell & Co. v. Local Union 304A, United Food & Commercial Workers, 913 F.2d 544, 563-64 (8th Cir. 1990) (Morrell) (finality in the context of issue preclusion may be satisfied where the litigation has reached such a stage that "the court sees no really good reason for permitting it to be litigated again"), cert. denied, 500 U.S. 905 (1991). However, although we agree in theory with the bankruptcy court's view that Cochrane could be collaterally bound by the state trial court's disposition of the legal issues underlying his claim that Tudor Oaks lacked the capacity to maintain its litigation against him, we decline to apply principles of issue or claim preclusion in the present appeal because the capacity-to-sue defense that has been raised in this bankruptcy case is materially different from the capacity-to-sue defense that was untimely raised (and thus waived) in the underlying state court action. Cochrane's state court capacity-to-sue defense, which he belatedly raised in his independent state court action, asserted that Tudor Oaks lacked the capacity to continue pursuing the underlying state

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[5]Actually, at the time the bankruptcy court filed its opinion on March 30, 1995, the Minnesota Court of Appeals had, unbeknownst to the bankruptcy court, only two days earlier affirmed the state trial court's order dismissing Cochrane's independent state court action. Cochrane v. Tudor Oaks Condominium Project, 529 N.W.2d 429, 436 (Minn. Ct. App. 1995) (affirming on the ground that Cochrane, "by failing to challenge Tudor Oak's capacity to sue throughout protracted litigation, waived [his] right to that challenge").

court litigation after Tudor Oaks dissolved. By contrast, in the present case, Cochrane is now challenging Tudor Oaks's post-dissolution capacity to bring an adversary proceeding to avoid the discharge of a debt in federal bankruptcy court. Thus, we focus on the bankruptcy court's primary rationale on this issue, that "[r]egardless of whether the named party-plaintiff [i.e., Tudor Oaks] is a valid, subsisting legal entity with capacity to sue or be sued, its one remaining partner has a right under Ontario law to wind up the affairs and to continue litigation under its name to do so." We review this rationale on the merits.

Upon de novo review, we apply Ontario law in determining whether Tudor Oaks had the capacity to bring the present bankruptcy litigation. The Ontario Partnership Act, § 38, provides in relevant part:

> After the dissolution of a partnership, the authority of each partner to bind the firm and other rights and obligations of the partners continue despite the dissolution so far as is necessary to wind up the affairs of the partnership and to complete transactions begun but unfinished at the time of the dissolution.

Applying the above-quoted standard to the circumstances of the present case, we agree with the bankruptcy court that McLaughlin's efforts in bringing this adversary proceeding on behalf of Tudor Oaks constitutes a

partner's exercise of rights "necessary to wind up the affairs of the partnership and to complete transactions begun but unfinished at the time of the dissolution." Thus, McLaughlin has standing to litigate this bankruptcy matter in the name of Tudor Oaks.

Application of collateral estoppel to factual issues

Next, Cochrane argues that the bankruptcy court erred in holding that, according to principles of collateral estoppel, he is bound by certain factual findings made in the underlying state court action. He maintains that those findings have no preclusive effect because he was denied a full and fair opportunity to litigate the pertinent issues. As to the three jury findings identified by the bankruptcy court, which involved instances where Cochrane breached fiduciary duties to his clients, Cochrane argues that there was no factual basis for the bankruptcy court's findings. He also argues that there was never any finding as to whether the state court judgment was obtained by fraud.

We hold that the bankruptcy court did not err in applying the doctrine of collateral estoppel to the jury's findings regarding Cochrane's breach of fiduciary duties. To begin, it is now well settled that "the principle of collateral estoppel applies in bankruptcy court to bar the relitigation of factual or legal issues that were determined in a prior state court action." Johnson v. Miera (In re Miera), 926 F.2d 741, 743 (8th Cir. 1991) (citing Grogan v. Garner, 498 U.S. 279

(1991)). In order for a factual issue to be barred from relitigation in a subsequent proceeding, the following four elements must be present: (1) "the issue sought to be precluded must be the same as that involved in the prior action"; (2) "the issue must have been litigated in the prior action"; (3) "the issue must have been determined by a valid and final judgment"; and (4) "the determination must have been essential to the prior judgment." Id. In the present case, issues concerning Cochrane's breach of his fiduciary duties were fully, fairly, and actually litigated and were essential to the final judgment entered in the underlying state court action. We therefore hold that the bankruptcy court did not err in concluding that Cochrane is bound by the jury's findings.

To the extent Cochrane argues that there was never a finding on the issue of whether the state court judgment was obtained by fraud, he is bound by the state trial court's findings in his independent state court action that -- with reference to the underlying state court action -- no fraud upon the court occurred in connection with Tudor Oaks's dissolution and, moreover, the judgment was not obtained by fraud. Cochrane v. Tudor Oaks Condominium Project, No. 93-16553, slip op. at 11-15 (Minn. Dist. Ct. July 6, 1994). Although the Minnesota Court of Appeals affirmed solely upon a finding of waiver, we hold that the above-noted fraud-related findings in Cochrane's independent state court action were final for purposes of applying the doctrine of

collateral estoppel because that litigation had reached such a stage that, in our view, there is "no really good reason for permitting [those issues] to be litigated again." Morrell, 913 F.2d at 563-64.

Nondischargeability under § 523(a)(4)

Cochrane challenges the bankruptcy court's legal conclusion that his conduct, which gave rise to the judgment in the underlying state court action, constituted fraud or "defalcation" within the meaning of 11 U.S.C. § 523(a)(4). Focusing primarily on the meaning of the term "defalcation," Cochrane argues that the bankruptcy court erred in interpreting the statute to include innocent or negligent misdeeds rather than solely intentional wrongs, such as fraud, embezzlement, or larceny. We disagree.

To begin, "[w]hether a relationship is a `fiduciary' one within the meaning of section 523(a)(4) is a question of federal law." Lewis v. Scott, 97 F.3d 1182, 1185 (9th Cir. 1996). "[T]he fiduciary relationship must be one arising from an express or technical trust that was imposed before and without reference to the wrongdoing that caused the debt." Id. In general, an attorney-client relationship is the type of relationship for which the attorney's breach of fiduciary duties to the client may give rise to a finding of a "defalcation" within the meaning of §523(a)(4). See, e.g., FDIC v. Mmahat, 907 F.2d 546, 550 (5th Cir. 1990), cert. denied, 499 U.S. 936 (1991). In the present case, Cochrane's

relationship with his clients existed before and notwithstanding the wrongdoing for which judgment against him was procured or, in other words, without reference to his wrongdoing. Cochrane had been engaged by Tudor Oaks and two Tudor Oaks partners to represent them in the bank foreclosure on Tudor Oaks's failing multimillion dollar condominium project. His clients understood that he would assemble a group of investors (i.e., KSCS) to buy out the project while allowing Tudor Oaks to retain a 20% interest. Cochrane instead kept the 20% interest for himself as a "fee" and also failed to disclose to his clients that he was a 25% shareholder in KSCS. He breached his fiduciary duties by failing to disclose his status as a KSCS shareholder and by usurping Tudor Oaks's expected 20% interest in the real estate, which, in fact, he kept for himself. In light of these facts, the bankruptcy court did not err in finding, for purposes of applying §523(a)(4), that he had committed an act by defalcation while acting in a fiduciary capacity. See, e.g., FDIC v. Mmahat, 907 F.2d at 550 (attorney who acted improperly to enrich himself at expense of his client was properly denied discharge of debt in bankruptcy under § 523(a)(4)).

We also reject Cochrane's argument that the bankruptcy court erroneously defined "defalcation" to include innocent or negligent misdeeds rather than solely intentional wrongs such as fraud, embezzlement, or larceny. While we doubt Cochrane could demonstrate that his acts were innocent

or merely negligent, that question is, in any event, not dispositive because a finding of "defalcation" does not require evidence of intentional fraud or other intentional wrongdoing.

> Defalcation is defined as the "misappropriation of trust funds or money held in any fiduciary capacity; [the] failure to properly account for such funds." Under section 523(a)(4), defalcation "includes the innocent default of a fiduciary who fails to account fully for money received." . . . An individual may be liable for defalcation without having the intent to defraud.

Lewis v. Scott, 97 F.3d at 1186 (citations omitted). The bankruptcy court did not err in holding that Cochrane's debt to Tudor Oaks resulted from an act of defalcation while acting in a fiduciary capacity. The judgment debt is nondischargeable pursuant to 11 U.S.C. § 523(a)(4).

Conclusion

For the reasons discussed above, we affirm the order of the district court affirming the bankruptcy court's grant of summary judgment in favor of Tudor Oaks on its claim that Cochrane's judgment debt is nondischargeable in bankruptcy pursuant to 11 U.S.C. § 523(a)(4).

A true copy.

Attest:

CLERK, U.S. COURT OF APPEALS, EIGHTH CIRCUIT.

UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

No. 96-1544MNST

Tudor Oaks Limited Partnership,	*	Appeal from the
Appellee,	*	U. S. District
v.	*	Court for the
John Alexander Cochrane,	*	District of
Appellant	*	Minnesota

ORDER

Appellant's motion for stay of mandate pending filing of writ of certiorari has been considered by the court and is denied.

November 17, 1997

Order Entered at the Direction of the Court:
/s/ Michael E. Gans
Clerk, U. S. Court of Appeals, Eighth Circuit

APPENDIX B

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MINNESOTA
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UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF MINNESOTA
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UNITED STATES DISTRICT COURT
DISTRICT OF MINNESOTA
THIRD DIVISION

In re
John Alexander Cochrane, Debtor

Appellant,

ORDER

vs.

Civ. File No. 3-95-389
Tudor Oaks Limited Partnership, Bky File No. 93-32056

Appellee.

This matter is before the court upon Appellant's appeal from Bankruptcy Judge Gregory F. Kishel's Order dated March 29, 1995. This court has jurisdiction pursuant to 28 U.S.C. §158(a). On appeal to the district court, the bankruptcy court's legal conclusions are subject to de nova review. In re Apex Oil, 884 F.2d 343 (8th Cir. 1989). The bankruptcy court's findings of fact are subject to a clearly erroneous standard of review. Bankruptcy Rule 8013.

Based on a review of the record and consideration of the submissions of the appellant and appellee, the court

concludes that Bankruptcy Judge Kishel's order is neither clearly erroneous nor contrary to law.

ORDER

Bankruptcy judge Gregory F. Kishel's order and final judgment dated March 29, 1995 is AFFIRMED.

Date: 2/6/96

/s/ Michael J. Davis
United States District Judge

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA
THIRD DIVISION

In re:
JOHN ALEXANDER COCHRANE,

Debtor

ORDER GRANTING FOR SUMMARY JUDGMENT

TUDOR OAKS LIMITED PARTNERSHIP,

Plaintiff,

BKY 3-93-2056

ADV 3-94-101

v.

JOHN A. COCHRANE,

Defendant.

At St. Paul, Minnesota, this 29th day of March, 1995.

This Adversary proceeding came on before the Court on December 13, 1994, for hearing on the Plaintiff's motion for summary judgment. The Plaintiff appeared by its attorney, William J. Fisher. The Defendant appeared by his

attorney, Michael J. Iannacone. Upon the moving and responsive documents and the arguments and legal memoranda submitted by counsel, the Court grants the motion.

The Defendant is a petitioner under Chapter 7 before this Court.[1] The Defendant scheduled the Plaintiff as a creditor in his original Schedule F. The plaintiff's claim was first evidenced by a judgment that was entered in the Minnesota State District Court for the Fourth Judicial District, Hennepin County, after a trial by jury and pursuant to a July 7, 1992 order of that court.[2] Various post-judgment

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[1]On December 21, 1992 the Defendant filed a voluntary petition for reorganization under Chapter 11 in the United States Bankruptcy Court for the Middle District of Florida. On motion of a scheduled creditor, the at court (Paskay, C.J.) Ordered a change of venue to the District of Minnesota. On February 15, 1994, this court converted the Debtor's case to one under Chapter 7.

[2]On the Defendant's bankruptcy schedules and in the pleadings for the state court action, the Plaintiff was denominated, respectively, as "Tudor Oaks Condo Project" and Tudor Oaks Condominium Project." In the state-court pleadings, the phrase "an Ontario Limited Partnership" was added to that cognomen. These forms of name are different from the one with which the Plaintiff has identified itself in the caption to this adversary proceeding. To support one of his substantive defenses to this motion, the Defendant attempts to make much out of the difference. This point is nothing but quibbling over a non-material happenstance. A bit of sloppiness in drafting fully accounts for the difference; there is no proof of record to rebut the proposition that all of these names signify the same entity. Contrary to his

proceedings and an appeal by the Defendant then ensued. On appeal, the amount of the jury's award of damages to The plaintiff was modified. On remand, the Hennepin County District Court liquidated the debt fully and finally, in a judgment entered pursuant to a February 24, 1994 order.[3] Via this adversary proceeding, the Plaintiff seeks a determination that this debt is excepted from discharge in bankruptcy by operation of 11 U.S.C. §523(a)(4).[4]

The Plaintiff now moves for summary judgment on this request for relief, pursuant to Fed. R. Bankr, P. 7056.[5]

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attorney's insistence, the Defendant very well knows "who's suing [him] and where they're coming from."

[3]The record does not contain a copy of the judgment or of the clerk's notice of its entry, and the date on which the judgment itself was entered does not otherwise appear from the record.

[4]In pertinent part, this statute excepts from discharge in any debt "for fraud or defalcation while acting in a fiduciary capacity..."

[5]This rule makes Fed R. Civ. P.56 applicable to adversary proceedings in bankruptcy. In pertinent part, Fed. R. Civ. P. 56© provides that, upon a motion for summary judgment,

> [t]he judgment sought shall be rendered forthwith if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits [submitted in support of the motion], if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law.

The first requirement of Rule 56 is, of course, a lack of triable fact issues--"no genuine issue of material fact." To establish this, the Plaintiff relies entirely on the doctrine of collateral estoppel, or "issue preclusion."

As the Supreme Court has recognized, collateral estoppel does lie in bankruptcy proceedings, as to previously-adjudicated fact issues that are common elements of a prior case of action under nonbankruptcy law and of a nondischargeable debt under 11 U.S.C. §523(a). *Grogan v. Garner,* 498 U.S. 279, 284-285 n. 11(1991). Where pre-petition litigation between a complaining creditor and a debtor had produced fact adjudications of adequate specificity, a creditor may move for summary judgment on the basis of the prior findings of fact. The issue in such a motion is purely one of law --whether the findings made by the nonbankruptcy tribunal meet the precise legal requirements of the theory of nondischargeability on which the creditor relies. The Plaintiff frames its motion in this fashion, and only in this fashion.[6]

It is necessary, then, to first recite the pertinent facts

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[6]Obviously, if the state courts' findings do not match the elements of §523(a)(4), the motion must be denied. In that case, this adversary proceeding could still proceed to trial, where the issue would be presented for decision on the trial testimony and exhibits.

that were settled by the Minnesota state courts' decisions.[7]

At all relevant times, the Plaintiff was a limited partnership.[8] It purchased certain real estate in Eden Prairie, Minnesota, planning to develop a residential condominium project there. Some lending entity within the First Bank system provided financing to the Plaintiff for acquisition and/or construction, The project financially failed, as did may such real estate developments in the mid-and late 1980s. First Bank foreclosed its mortgage, and bid in at the June 12, 1985

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[7]The Hennepin County District Court (Larson, J.) Submitted the state-court plaintiffs' three claims of breach of fiduciary duty to the jury on special interrogatories. Three of these interrogatories addressed whether the Defendant had breached a fiduciary duty to the Plaintiff in separate alleged instances. The jury answered in the affirmative to all three. In his July 7, 1992 order for judgment, Judge Larson merged these answers into findings of fact. Then, in its unpublished opinion, the Minnesota Court of Appeals recited the factual backdrop in some detail, summarizing the parties' legal and contractual relationships and the history of the transactions that gave rise to the Plaintiff's claim. *S.B. McLaughlin & Co., Ltd., v. Cochrane,* C4-92-2081, slip op. At 2-3 (Minn. Ct.App. June 29, 1993). Most of the following recitation is taken from that opinion. Undoubtedly, the appellate court based its findings on the uncontroverted basic evidence presented at the trial, as well as any controverted evidence that properly supported the summary fact findings made in the jury's answers to special interrogatories.

[8]Though the Minnesota state courts did not specifically find as such, the Plaintiff was organized under the laws of the province of Ontario, Canada.

sheriff's sale for $5,600,000.00. It the prosecuted some sort of deficiency judgment action[9] against the Plaintiff and its liable partners.

The Defendant is an attorney at law licensed to practice in the state of Minnesota and numerous federal courts. He has substantial experience in complex business litigation. Two out of the Plaintiff's three partners retained him to represent themselves and the Plaintiff in defending the deficiency judgment action. Under the terms of engagement, the Defendant was to charge them a flat fee of $20,000.00.

Apparently, at some point early in the deficiency-judgement litigation , First Bank made an overture of settlement to the Defendant's clients. It offered to release the deficiency claims if the Defendant's clients aided the Bank's ultimate recovery by facilitating a sale of the underlying property.[10]

The Defendant the assembled a group of investors to purchase First Bank's rights under the sheriff's certificate of

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[9]This is the designation given by the Minnesota Court of Appeals in its opinion,. The record before this Court is silent as to may of the surrounding circumstances. If this designation was accurate, however, First Bank must have bid in at the sheriff's sale for an amount less than the outstanding debt chargeable against the property under the original loans.

[10]Obviously, in structuring the offer this way First Bank sought to rid itself of both the legal and the financial aftermath of its failed investment in the project, in one step, and at a substantial loss.

sale. The investors incorporated under the name KSCS Properties, Inc. ("KSCS"). The defendant did not disclose to his clients, the plaintiff and its partners, that he was a principal in KSCS, to the extent of owning 25 percent of its outstanding shares.

The Plaintiff, the two client-partners, and the Defendant then arrived at separate terms of engagement for his services in connection with the contemplated sale of the rights under the sheriff's certificate. As this second phase of the retention went forward, the Plaintiff's partners all expected that the Plaintiff would retain a 20 percent fractional ownership in the post-closing configuration of property rights in the underlying real estate.[11] Ultimately, however, the Defendant brokered a transaction which led to the following results:

1. The Defendant's clients agreed that he would receive a 20 percent fractional ownership interest in the underlying real estate, as his fee for finding a purchaser and negotiating and

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[11]The record before this Court does not reveal just how the real estate was to be held after the closing--"direct" ownership by a group of named grantees, or through a new grantee-entity in which participants would hold equity interests. The omission is not material, but it requires some vagueness in describing just what was to come out of the whole transaction.

closing the sale of the sheriff's certificate, and he did receive such a share;

2. KSCS took a 60 percent ownership interest in the real estate; and

3. Two of KSCS's other shareholders, Rolland Stinski and Bill Keifer, Sr., took title to the final 20 percent ownership interest in the real estate, in their individual right.

Apparently, the purchase of the sheriff's certificate and the reconfiguration of ownership interests in the real estate closed in fairly short order.

At some point after that closing, the Plaintiff's principals discovered the extent of the Defendant's involvement and interest in KSCS. In 1987, the Plaintiff and two of this partners sued the Defendant in Hennepin County District Court. They alleged that they had suffered substantial damages as a result of a breach of fiduciary duty on the part of the Defendant. The action consumed years of litigation, including an abortive removal of the lawsuit to the United States District Court for this District, a remand, and several motions for summary judgment. Finally it went to trial in mid-1992. In its answers to special interrogatories, the jury found that the Defendant had breached a fiduciary duty to the Plaintiff in three instances: by personally participating in the

purchase of the Sheriff's certificates as a shareholder in KSCS, by his involvement in a transaction that defeated the Plaintiff's expectation that it would retain the 20 percent fraction interest in the real estate; and by charging a 20 percent contingency fee for his services in the second phase of the retention.

In its opinion, the Minnesota Court of Appeals analyzed the jury's award of damages at some length, and then reduced the award of damages to the Plaintiff from the Defendant by approximately $400,000.00.[12] It affirmed the jury's finding of causation between the Defendant's adjudged breach of fiduciary duty and the injury The plaintiff suffered. After disposing of numerous other issues raised by the Defendant,[13] it remanded. On remand, Judge Larson analyzed the jury's verdict and the extant evidence in light of the rulings of the Court of Appeals, and ordered entry of the judgment as to which dischargeability is in dispute here.

The issue presented on this motion is actually quite simple: do the facts as found by the state courts demonstrate a "defalcation while acting within a fiduciary capacity" within the meaning of §523(a) (4)? If they do, the Plaintiff wins.

It has long been the law that the "fiduciary" status in

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[12]It also reversed that portion of the trial court's judgment that had held the Defendant directly and additionally liable to one of the Plaintiff's general partners in its individual right.

[13]Apparently, the Defendant did not designate the jury's basic finding of breach of fiduciary duty as an issue for his appeal.

question under §523(a)(4) must arise under an express, pre-existing trust. *Davis v. Aetna Acceptance Co.*, 293 U.S. 238, 33 (1934) (decided under analog to §523(a)(4) in Bankruptcy Act of 1898); *In re Dloogoff*, 600 F.2d 166, 170 (8th Cir.1979) (ditto); *In re Long*, 774 F.2d 875, 878 (8th Cir. 1985); *In re Koelfgen*, 87 B.R. 993, 996 (Bankr.D.Minn.1988); *In re Crea*, 31 B.R. 239, 244 (Bankr.D.Minn. 1983). "The (Bankruptcy) Code does not reach constructive trustees, designated as such because of misconduct." *In Re Long*, 774 F.2d at 878. *See also In re Crea*, 31 B.R. at 244. The fiduciary relationship, then, must have been created before the acts complained of *In re Barker*, 40 B.R. 356, 358-359 (Bankr.D.Minn. 1984).

Federal bankruptcy law, then, limits the concept of "fiduciary" to persons acting under an objectively manifested, pre-existing, and binding relationship. However, the threshold existence of that relationship--whether arising under an indenture of trust or otherwise--is controlled by state law. *In re Bennet*, 989 F.2d 779, 784 (5th Cir. 1993); *Ragsdale v. Haller*, 780 F.2d 794, 796 (9th Cir. 1986); *In re Interstate Agency, Inc.*, 760 F.2d 121, 124 (6th Cir. 1985) (decided under Bankruptcy Act of 1898); *In re Pedrazzini*, 664 F.2d 756, 758 (9th Cir. 1981) (ditto); *In re Angelle*, 610 F.2d 1335, 1341 (5th Cir. 1980) (ditto).

Over eighty years ago the Minnesota Supreme Court noted that

> [i]t is well settled that the obligation of fidelity which an attorney owes to his client is a continuing one, and that he cannot make use of any knowledge acquired from his client, or through his professional relation, for his own advantage, adverse to the interests of his client, or those claiming through him...

Sanfrod v. Flint, 108 Minn.399, 401, 122 N.W. 315 (1909). More to the point, and more recently, it held:

> The relation between an attorney and his client is *a fiduciary one of the highest trust and confidence* and, as long as the relationship of the influence thereof exists, requires the attorney to observe the utmost good faith and candor and *not to allow his private interest to conflict with those of his client.* The relation places the attorney under no legal disability in dealing with his client but simply imposes on him a *much high standard of good faith* than is required in business dealings where the parties trade at arms-length. Where the relationship exists, *these strict rules of fiduciary conduct* cast upon the attorney the burden of proving that he has been absolutely frank and fair with his client and has taken no advantage of the confidence arising from such professional relation.

Colstad v. Levine, 243 Minn. 279, 286-287, 67 N.W.2d 648, 654 (1954) (emphasis added; emphasis that was in original,

and citations in original, deleted). As a general proposition, any transaction by which an attorney acquires property from his client is discouraged, and is subject to close scrutiny. In such transactions,

> [t]he burden of proving entire fairness, adequacy of consideration and absolute good faith, is put upon the attorney.

Mercer v. McHie, 141 Minn. 144, 146, 169 N.W. 531 (1918).

Clearly, then, under Minnesota law, an attorney is utterly prohibited from self-dealing in the subject matter of his retention, to the detriment of an unknowing client. At its heart, this is a defined obligation not to elevate the attorney's self-interest over his client's interests. This is the very essence of a fiduciary duty. The jury in the Hennepin County District Court action unquestionably found that the Defendant had breached this duty of fidelity and good faith to the Plaintiff.

The Defendant obdurately denies that this adjudicated breach equates to the "defalcation" contemplated by §523(a)(4). He makes two arguments on this point. Both of them lack merit.

First, contrary to the Defendant's argument, there need not be an "express trust" within the strict definition of nonbankruptcy law, for there to have been a "fiduciary capacity" cognizable under §523(a)(4).

In all fairness on this point, one must acknowledge that the Defendant "held nothing in trust," as his counsel points out. The Plaintiff and its partners never gave him control over a defined trust *res,* whether in the form of a retainer or an escrow, and they never named him as a trustee in a written instrument creating a formal trust.[14] Beyond that--though, admittedly, it is irrelevant to the present analysis--the Minnesota state courts denied his clients' request for the imposition of a constrictive trust against the subject real estate. Too, in passing on the existence of fiduciary capacity in the cases before them, virtually all of the reported decisions under §523(a)(4) from the District of Minnesota and the Eight Circuit make reference to the elements of a formal trust under nonbankruptcy law. *In re Long,* 774 F.2d at 878; *In re Dloogoff,* 600 f.2d at 169-170; *In re Koelfgen,* 87 B.R. at 996-997; *In re Barker,* 40 B.R. at 359; *In re Crea,* 31 B.R. at 244-245.

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[14]In *In re Bush's Trust*, 249 Min. 36, 81 N.W.2d 615 (1957), the elements of an express trust under Minnesota law were identified as:

> ...(1) a designated trustee subject to enforceable duties, (2) a designated beneficiary vested with enforceable rights, and (3) a definite trust *res* wherein the trustee's title and estate is separated from the vested beneficial interest of the beneficiary...

249 Minn. At 43, 81 N.W.2d at 620. *See also Schug v. Michael,* 310 Minn. 22, 27, 245 N.W.2d 587, 590-591 (1976).

However, as a matter of the same nonbankruptcy law, one thing is absolutely clear: the concept of "fiduciary" is broader than the concept of "trustee under an express trust."[15] The pronouncement quoted from *Colstad v. Levin* clearly is to this effect; it recognized that an attorney is often put into a position of relative power over a client's options and opportunities. The manipulation of that power to benefit the attorney at the expense of the client is strictly forbidden. Such positions of power do not always involve the deposit of identified assets in trust with the attorney. Correspondingly, the professional's fiduciary duty of forbearance is not limited to situations involving segregated, entrusted assets. *See* Janet

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[15]Put another way: while a trustee under an express trust is always a fiduciary, a fiduciary need not always be a trustee under an express trust. Many Bankruptcy Courts have agreed with this general proposition, on rationales that vary greatly In their degree of development and in the extent to which they rely on cited state-law authority. *E.g., In re Brown,* 131 B.R. 900, 905 (Bankr. D. Me. 1991) (corporate officer's misapplication of company's assets to his personal debts gave rise to debt nondischargeable under §523(a)(4), where "In general state law sense" he had been fiduciary to company); *In re Sax,* 106 B.R. 534, 538 (Bankr. N.D. Ill. 1989) (former director and controlling shareholder of failed bank breached fiduciary duty when he obtained loans from bank for his own business corporation without board authorization and in violation of lending guidelines; debt held nondischargeable); *In re Godlen,* 54 B.R. 957, 964 (Bankr. D. Mass. 1985) (acts of corporation's sales agent in accepting "kickbacks" from trade vendor and taking clandestine "consulting" job with vendor, gave rise to nondischargeability under §523(a)(4), as did misapplication of employer's funds earmarked for payment of trade payables).

A. Flaccus, *Attorney Malpractice Judgments, Bankruptcy Discharge, and Professional Responsibility,* 4 J. Bankr. L. & Pract. 219, 227 (1995).

Recognizing the special nuances of the attorney-client relationship, virtually all of the Bankruptcy Courts that have reported decisions involving the dischargeability of debts owning by debtor-attorneys to their former clients have held, expressly or tacitly, that an attorney's generalized professional duties of fidelity, good faith, and "utmost fairness" to a client are sufficient in themselves to place the attorney into a "fiduciary capacity" cognizable under §523(a)(4) as to the subject matter of the retention. *F.D.I.C. v. Mmahat*, 907 F.2d 546, 549-550 (5th Cir. 1990), *aff'g* 97 B.R. 293, 296 (E.D. La. 1988), *cert. den.*, 499 U.S. 936 (1991) (breaches of fiduciary duty of attorney/board member for failed financial institution, in advising board to make improvident loans from which his law firm made substantial fees in transactions, gave rise to a debt nondischargeable under §523(a)(4)); *Kwiat v. Doucette*, 81 B.R. 184, 188-189 (D.Mass 1987) (nondischargeable debt created by attorney's knowing breach of terms of retention agreement with client, where client's tort recovery had been substantially reduced by amount of fees that attorney had agreed to recover independently from opposing party); *In re McDowell*, 162 B.R. 136, 137 (Bankr. N.D. Ohio 1993) (sequence of wrongdoing by attorney in relation to prosecution of tort claims and disposition of proceeds of settlement, resulting in

loss of client's recovery, was defalcation by fiduciary under §523(a)(4)); *In re Kudla*, 105 B.R. 985, 990-991 (Bankr. D. Colo. 1989) (failure to preserve $100,000.00 deposited in trust breached "highest standard of fiduciary obligations," which law imposes on attorney-client relationship, mandating determination of nondischargeability); *In re Janikowski*, 60 B.R. 784, 790 (Bankr. N.D. Ill. 1986) (attorney's failure to record deeds and instruments entrusted to him may consitute defalcation by fiduciary under §523(a)(4), given dictate of state law that attorneys maintain "fidelity to clients with an eye single to their best interests"). *Cf. In re Gans*, 75 B.R. 474, 491-492 (Bankr. S.D.N.Y.) (Where debt in question was result of personal loan from client to lawyer and transaction did not come out of attorney-client relationship, debt is not excepted from discharge by §523(a)(4)).

These decision all fully comport with the Congressional intent that appears with utter clarity from the very presence of §523(a)(4) in the Code: under American law, the sensitive relationship of a fiduciary to its beneficiary is so important that those who violate their duty of special trust under it are to be denied the refuge of discharge in bankruptcy, regardless of the origin of the nature of their breach. *See In re Baird*, 114 B.R. 198-204 (Bankr. 9th Cir. 1990) ("defalcation" within meaning of §523(a)(4) "includes innocent, as well as intentional or negligent defaults so as to reach the [wrongful] conduct of all fiduciaries. . ."); *In re Gonzales*, 22 B.R. 58, 59 (Bankr. 9th Cir. 1982); *In re*

Anderson, 64 B.R. 331, 334 (Bankr. N.D. Ill. 1986).

For basically the same reason, the Defendant's second substantive argument also fails. The Defendant argue, at some length but in a rather unfocused fashion, that the "mere breach of fiduciary duty" adjudicated in the Minnesota courts does not rise to the level of "defalcation" proscribed by §523(a)(4). This argument has been rejected for over fifty years:

> Colloquially perhaps the word, 'defalcation,' ordinarily implies some moral dereliction, but in this context it may have included innocent defaults, so as to include all fiduciaries who for any reason were short in their accounts. . . . Whatever was the original meaning of 'defalcation' it must have covered other defaults than deliberate malversations, else it added nothing to the [other] words [in the statute], 'fraud or embezzlement."

Central Hanover Bank & Trust Co. v. Herbst, 93 F.2d 510, 511 (2d Cir. 1937) (L. Hand, J.) (examining history of statutory predecessor of §523(a)(4) in Bankruptcy Act of 1898, back to Bankruptcy Act of 1800). Elaborating on this thought, numerous courts have declined to require a complaining creditor to prove that the defalcating fiduciary harbored malice, ill-will, fraud, or other specific intent to cause harm to this beneficiary. They have limited this principle in various formulations. *See, e.g., In re Bennett*, 989

F.2d at 790 (defining defalcation as "willful neglect of duty" that need not be "accompanied by fraud or embezzlement"); *In re Moreno*, 892 F.2d 417, 421 (5th Cir. 1990) (ditto); *American Inc. Co. v. Lucas*, 41 B.R. 923, 925 (W.D. Pa. 1984); *Martino v. Brown*, 34 B.R. 116, 117 (D.N.M. 1983); *In re Baird*, 114 B.R. at 204, *In re Crosswhite*, 91 B.R. 156, 160 (Bankr. M.D. Fla. 1988) (defalcation may occur "even where the merest deficit is caused by "fiduciary's conduct, and even where fiduciary has not derived benefit from shortage); *In re Mullin*, 91 B.R. 175, 176 (Bankr. S.D. Fla. 1988) (finding of defalcation "does not require intentional conduct"); *In re Kelly*, 84 B.R. 225, 230 (Bankr. M.D. Fla. 1988) ("no element of intent or bad faith need . . . be shown" for determination that defalcation has taken place); *In re Pavelka*, 79 B.R. 228, 232 (Bankr. E.D. Pa. 1987) ("[n]o specific intent is necessary to find" defalcation under §523(a)(4)); *In re Codias,* 78 B.R. 344, 346 (Bankr. S.D. Fla. 1987) (defalcation may be established even where fiduciary had committed only negligence or ignorance); *In re Anderson*, 64 B.R. at 334 (defalcation "includes innocent defaults in duty"). *Cf. Meyer v. Rigdon*, 36 F.3d 1375. 1382-1385 (7th Cir. 1994) (applying 11 U.S.C. §523(a)(11); collecting cases, and concluding that "mere negligent breach of a fiduciary duty" is not "defalcation" as contemplated by that provision).

It is clear, then, that the Minnesota state courts' unadorned finding that the Defendant had breached his fiduciary duty to the Plaintiff in three separate instances is

sufficient to make out a "defalcation" within the contemplation of §523(a)(4).[16] This conclusion seems particularly merited in a case involving an attorney-debtor and a client-creditor: given the special trust inherent in the underlying relationship, the key aspect of the analysis under §523(a)(4) should be on the compromise of loyalties--not on the finesses, subjective rationale that the attorney may have used to justify it to himself.

There are no other issues that deserve extended discussion.[17] This all means, then, that the debt that the

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[16]One can reach this conclusion without having to decide whether the threshold for intent is the negligible one of "innocence" or "ignorance" in the default, or the more challenging one of "willfulness" in the neglect of fiduciary duty; the record meets the latter standard. "Willfulness" is generally defined as deliberateness in action, rather than negligence. *In re Long*, 774 F.2d at 880. (Though the *Long* court adopted this definition for its analysis of a court under 11 U.S.C. §523(a)(6), it really was doing no more than adopting a common definition used in many areas of American law.) The Defendant cannot deny that he acted knowingly and deliberately to et up KSCS, to participate in it, and to shepherd the transaction to fruition, and he does not do so. Whatever the characterization to be placed on a debtor's *scienter* for the purposes of §523(a)(4), the state court's findings satisfy it.

[17]As he has (without success) in earlier proceedings in his main bankruptcy case, the Defendant maintains that the named Plaintiff lacks standing to obtain relief here because it was dissolved by operation of Ontario law before his bankruptcy filing. This argument is a red herring. Regardless of whether the named party-plaintiff is a valid, subsisting legal entity with capacity to sue

Minnesota state courts reduced to judgment is excepted from discharge in bankruptcy.

IT IS THEREFORE ORDERED, ADJUDGED AND DECREED:

1. That the Plaintiff's motion for summary judgment is granted.

2. That the Defendant's debt to the Plaintiff, as reduced to judgment by the Minnesota State District Court for the Fourth Judicial District, Hennepin County, pursuant to an order for judgment dated February 24, 1994, under the caption of *S.B. McLaughlin & Company, Ltd., v. John Cochrane, et al,* Court File No. 87-

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or to be sued, its one remaining partner has a right under Ontario law to wind up its affairs and to continue litigation under its name to do so. During the pendency of this adversary proceeding, the Hennepin County District Court held to that effect, in ruling against the Defendant in his independent lawsuit for relief from the original judgment in the Plaintiff's favor. *Cochrane v. Tudor Oaks Condominium Project, et al.*, No. 93-16553, Memorandum Order Granting Defendant's Motion for Summary Judgment at 14-15 (Minn. State D. Ct., 4th Jud. Dist. July 6, 1994). The Defendant is collaterally bound by this ruling, *In re Miera*, 925 F.2d 741, 743 (8th Cir. 1991), even though he apparently has an appeal from that judgment pending, *Robi v. Five Platters, Inc.*, 838 F.2d 318, 327 (9th Cir. 1988).

11035, was excepted from the discharge in bankruptcy granted to the Defendant on May 24, 1994, in BKY 3-93-2056, by operation of 11 U.S.C. §523(a)(4).

LET JUDGMENT BE ENTERED ACCORDINGLY.

BY THE COURT:

/S/ Gregory F. Kishel

GREGORY F. KISHEL
U.S. BANKRUPTCY JUDGE

APPENDIX C

RELEVANT STATUTES

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RELEVANT STATUES

11 U.S.C. § 523. Exceptions to discharge

(a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt--

(1) for a tax or a customs duty--

(A) of the kind and for the periods specified in section 507(a)(2) or 507(a)(8) of this title, whether or not a claim for such tax was filed or allowed:

(B) with respect to which a return, if required--

(I) was not filed; or

(ii) was filed after the date on which such return was last due, under applicable law or under any extension, and after two years before the date of the filing of the petition; or

(C) with respect to which the debtor made a fraudulent return or willfully attempted in any manner to evade or defeat such tax;

(2) for money, property, services, or an extension , renewal or refinancing of credit, to the extent obtained by--

(A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition;

(B) use of a statement in writing--

(I) that is materially false;

(ii) respecting the debtor's or an insider's financial condition;

(iii) on which the creditor to whom the debtor is liable for such money, property, services, or credit reasonably relied; and

(iv) that the debtor caused to be made or published with intent to deceive; or

(C) for purposes of subparagraph (A) of this paragraph, consumer debts owed to a single creditor and aggregating more than $1,000 for "luxury goods or services" incurred by an individual debtor on or within 60 days before the order for relief under this title, or cash advances aggregating more than $1,000 that are extensions of consumer credit under an open

end credit plan obtained by an individual debtor on or within 60 days before the order for relief under this title, are presumed to be nondischargeable; "luxury goods or service" do not include goods or services reasonably acquired for the support or maintenance of the debtor or a dependent of the debtor; an extension of consumer credit under an open end credit plan is to be defined for purposes of this subparagraph as it is defined in the Consumer Credit Protection Act;

(3) neither listed nor scheduled under section 521(1) of this title, with the name, if known to the debtor, of the creditor to whom such debt is owed, in time to permit--

(A) if such debt is not of a kind specified in paragraph (2), (4), or (6) of this subsection, timely filing of a proof of claim, unless such creditor had notice or actual knowledge of the case in time for such timely filing; or

(B) if such debt is of a kind specified in paragraph (2), (4), or (6) of this subsection, timely filing of a proof of claim and timely request for a determination of dischargeability of such debt under one of such paragraphs, unless such creditor had notice or actual knowledge of the case in time for such timely filing and request;

(4) for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny;

(5) to a spouse, former spouse, or child of the debtor, for alimony to, maintenance for, or support of such spouse or child, in connection with a separation agreement, divorce decree or other order of a court of record, determination made in accordance with State or territorial law by a governmental unit, or property settlement agreement, but not to the extent that--

(A) such debt is assigned to another entity, voluntarily, by operation of law, or otherwise (other than debts assigned pursuant to section 408(a)(3) of the Social Security Act, or any such debt which has been assigned to the Federal Government or to a State or any political subdivision of such State); or

(B) such debt includes a liability designated as alimony, maintenance, or support, unless such liability is actually in the nature of alimony, maintenance, or support;

(6) for willful and malicious injury by the debtor to another entity or to the property of another entity;

(7) to the extent such debt is for a fine, penalty, or

forfeiture payable to and for the benefit of a governmental unit, and is not compensation for actual pecuniary loss, other than a tax penalty--

(A) relating to a tax of a kind not specified in paragraph (1) of this subsection; or

(B) imposed with respect to a transaction or event that occurred before three years before the date of the filing of the petition;

(8) for an educational benefit overpayment or loan made, insured or guaranteed by governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution, or for an obligation to repay funds received as an educational benefit, scholarship or stipend, unless--

(A) such loan, benefit, scholarship, or stipend overpayment first became due more than 7 years (exclusive of any applicable suspension of the repayment period) before the date of the filing of the petition; or

(B) excepting such debt from discharge under this paragraph will impose an undue hardship on the debtor and the debtor's dependents;

(9) for death or personal injury caused by the debtor's operation of a motor vehicle if such operation was unlawful because the debtor was intoxicated from using alcohol, a drug, or another substance;

(10) that was or could have been listed or scheduled by the debtor in a prior case concerning the debtor under this title or under the Bankruptcy Act in which the debtor waived discharge, or was denied a discharge under section 727(a)(2), (3), (4), (5), (6), or (7) of this title, or under section 14c(1), (2), (3), (4), (6), or (7) of such Act;

(11) provided in any final judgment, unreviewable order, or consent order or decree entered in any court of the United States or of any State, issued by a Federal depository institutions regulatory agency, or contained in any settlement agreement entered into by the debtor, arising from any act of fraud or defalcation while acting in a fiduciary capacity committed with respect to any depository institution or insured credit union;

(12) for malicious or reckless failure to fulfill any commitment by the debtor to a Federal depository institutions regulatory agency to maintain the capital of an insured depository institution, except that this paragraph shall not extend any such commitment which would otherwise be terminated due to any act of such agency; or

(13) for any payment of an order of restitution issued under title 18, United States Code;

(14) incurred to pay a tax to the United States that would be nondischargeable pursuant to paragraph (1);

(15) not of the kind described in paragraph (5) that is incurred by the debtor in the course of a divorce or separation or in connection with a separation agreement, divorce decree or other order of a court of record, a determination made in accordance with State or territorial law by a governmental unit unless--

(A) the debtor does not have the ability to pay such debt from income or property of the debtor not reasonably necessary to be expended for the maintenance or support of the debtor or a dependent of the debtor and, if the debtor is engaged in a business, for the payment of expenditures necessary for the continuation, preservation, and operation of such business; or

(B) discharging such debt would result in a benefit to the debtor that outweighs the detrimental consequences to a spouse, former spouse, or child of the debtor;

(16) for a fee or assessment that becomes due and payable after the order for relief to a membership association with respect to the debtor's interest in a dwelling unit that has condominium ownership or in a share of a cooperative housing corporation, but only if such fee or assessment is payable for a period during which--

(A) the debtor physically occupied a dwelling unit in the condominium or cooperative project; or

(B) the debtor rented the dwelling unit to a tenant and received payments from the tenant for such period, but nothing in this paragraph shall except from discharge the debt of a debtor for a membership association fee or assessment for a period arising before the entry of the order for relief in a pending or subsequent bankruptcy case;

(17) for a fee imposed by a court for the filing of a case, motion, complaint, or appeal, or for other costs and expenses assessed with respect to such filing, regardless of an assertion of poverty by the debtor under section 1915(b) or (f) of title 28, or the debtor's status as a prisoner, as defined in section 1915(h) of title 28; or

(18) owed under State law to a State or municipality that is--

(A) in the nature of support, and

(B) enforceable under part D of title IV of the Social Security Act (42 U.S.C. 601 et seq.).

(b) Notwithstanding subsection (a) of this section, a debt that was excepted from discharge under subsection (a)(1), (a)(3), or (a)(8) of this section, under section 17a(1), 17a(3), or 17a(5) of the Bankruptcy Act, under section 439A of the Higher Education Act of 1965, or under section 733(g) of the Public Health Service Act in a Prior case concerning the debtor under this title, or under the Bankruptcy Act, is dischargeable in a case under this title unless, by the terms of subsection (a) of this section, such debt is not dischargeable in the case under this title.

(c)(1) Except as provided in subsection (a)(3)(B) of this section, the debtor shall be discharged from a debt of a kind specified in paragraph (2), (4), (6), or (15) of subsection (a) of this section, unless, on request of the creditor to whom such debt is owed, and after notice and a hearing, the court determines such debt to be excepted from discharge under paragraph (2), (4), (6), or (15), as the case may be, of subsection (a) of this section.

(2) Paragraph (1) shall not apply in the case of a Federal depository institutions regulatory agency seeking, in its capacity as conservator, receiver, or liquidating agent for an insured depository institution, to recover a debt described in subsection (a)(2), (a)(4), (a)(6), or (a)(11) owed to such institution by an institution-affiliated party unless the receiver, conservator, or liquidating agent was appointed in time to reasonably comply, or for a Federal depository institutions regulatory agency acting in its corporate capacity as a successor to such receiver, conservator, or liquidating agent to reasonably comply, with subsection (a)(3)(B) as a creditor of such institution-affiliated party with respect to such debt.

(d) If a creditor requests a determination of dischargeability of a consumer debt under subsection (a)(2) of this section, and such debt is discharged, the court shall grant judgement in favor of the debtor for the costs of and a reasonable attorney's fee for, the proceeding if the court finds that the position of the creditor was not substantially justified, except that the court shall not award such costs and fees if special circumstances would make the award unjust.

(e) Any institution-affiliated party of a insured depository institution shall be considered to be acting in a fiduciary capacity with respect to the purposes of subsection (a)(4) or (11).

28 § 1738: STATE AND TERRITORIAL STATUTES AND JUDICIAL PROCEEDINGS: FULL FAITH AND CREDIT.

The Acts of the legislature of any State, Territory of Possession of the United States, or copies thereof, shall be authenticated by affixing the seal of such State, Territory or Possession thereto.

The records and judicial proceedings of any court of any such State, Territory, or Possession or copies thereof, shall be proved or admitted in other courts within the United States and its Territories and Possessions by the attestation of the clerk and seal of the court annexed, if a seal exist, together with a certificate of a judge of the court that the said attestation is in proper form.

Such Acts, records and judicial proceedings or copies thereof, so authenticated, shall have the same full faith and credit in every court within the United States and its Territories and Possessions as they have by law or usage in the courts of such State, Territory or Possession from which they are taken. (June 25, 1948, c. 646, 62 Stat. 947)

APPENDIX D

RELATED STATE COURT ACTIONS

COURT OF APPEAL OF MINNESOTA

Appletree Square I v. O'Connor & Hannan
559 N.W. 2d 711 (Minn.App. 1997); *Page 52*

Cochrane v. Tudor Oaks Condominium Project
529 N.W.2d 429 (Minn.App. 1995); *Page 60*

S.B. McLaughlin & Co., et al. v. Cochrane, et al.
June 23, 1993; Page 99

STATE OF MINNESOTA DISTRICT COURT
FOURTH JUDICIAL DISTRICT

Cochrane v. Tudor Oaks Condominium Project
Order and Memorandum, July 6, 1994; Page 82

S.B. McLaughlin & Co., et al. v. Cochrane, et al.
Transcript of Proceedings (Partial)
June 2, 1992; Page 114

APPLETREE SQUARE I LIMITED PARTNERSHIP AND BUSINESS CONSULTANTS, INC. as Liquidating Agent for Appletree Square I, Limited Partnership, Respondents,

v.

O'CONNOR & HANNAN, a general partnership, et al., Appellants.

No. C2-96-1360

Court of Appeals of Minnesota.

March 4, 1997.

Bankrupt debtor and its liquidating agent brought malpractice action against debtor's former counsel. The District Court, Hennepin County, J. Thomas Mott, J., denied counsel's motion to dismiss, and counsel appealed. The Court of Appeals, Thomas G. Forsberg, J., held that Minnesota law prohibiting assignment of legal malpractice claims prohibited enforcement of malpractice claim of liquidating agent.

Reversed.

Syllabus by the Court

Because assignment of a legal malpractice claim is contrary to Minnesota public policy, a representative or liquidating agent appointed under the terms of a confirmed plan of liquidation does not have standing to assert a legal malpractice claim on behalf of a bankruptcy debtor against its former attorney.

Robert D. Brownson, Kristin Ottmar, Stich, Angell, Brownson & Ballou, P.A., Minneapolis, Richard L. Pemberton, Robert J. Sefkow, Pemberton, Sorlie, Sefkow, Ruffer & Kershner, P.L.L.P., Fergus Falls, Edward J. Laubach, Jr., Hall & Byers, P.A., St. Cloud, for Respondents.

James S. Simonson, Michael C. Flom, Gray, Plant, Mooty, Mooty & Bennet, P.A., Minneapolis, for Appellants.

Considered and decided by SCHUMACHER, P.J., TOUSSAINT, C.J., and FORSBERG,* J.

OPINION

THOMAS G. FORSBERG, Judge.

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*Retired judge of the Minnesota Court of Appeals, serving by appointment pursuant to Minn. Const. Art. VI § 10.

Respondents Appletree Square I Limited Partnership (Appletree) and Business Consultants, Inc., as Liquidating Agent for Appletree (BCI), brought this legal malpractice action against appellants O'Connor & Hannan and 56 of its former and present attorneys (O'Connor & Hannan). O'Connor & Hannan moved to dismiss the complaint, arguing that because legal malpractice claims are not assignable, the trial court lacked subject matter jurisdiction, BCI had no standing, and the complaint failed to state a claim upon which relief could be granted. The district court denied the motion, and this appeal followed.[1] Because legal malpractice claims are not assignable under Minnesota law, we reverse.

FACTS

In 1981, Appletree purchased a 15-story office building from the building's original owner and architect. During the building's construction in 1972 and 1973, an asbestos fireproofing material manufactured by W.R. Grace & Company had been sprayed on the steel support beams.

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[1]By order on July 16, 1996, this court concluded that the challenge by O'Connor & Hannan to BCI's authority to bring this legal malpractice claim was analogous to the subject matter jurisdiction challenge involved in *McGowan v. Our Savior's Lutheran Church*, 527 N.W.2d 830 (Minn.1995). The district court's order is, therefore, appealable as a matter of right.

In 1990, Appletree and its general partners retained O'Connor & Hannan to bring a federal action against W.R. Grace. The complaint alleged a RICO violation, as well as several state law claims. The state law claims were dismissed as time-barred. *See Appletree Square I Ltd. Partnership v. W.R. Grace & Co.*, 815 F.Supp. 1266 (D.Minn.1993). By separate order, the RICO claim was also dismissed. *Id.*, Civ. No. 3-92-701 (D.Minn. 1993). These two rulings were affirmed by the Eighth Circuit Court of Appeals. *Id.*, 29 F.3d 1283 (8th Cir.1994).

On September 17, 1993, Appletree, again represented by O'Connor & Hannan, filed for federal bankruptcy protection under Title 11. A liquidating plan was proposed by Appletree's creditors and eventually approved by the bankruptcy court. Under the terms of that plan, one of the creditors was given authority to select a disinterested person to be the "Liquidating Agent." Prior to confirmation, the creditor notified the bankruptcy court that it had selected BCI. One business day after confirmation, the plan "vested" BCI, as the liquidating agent, with all of Appletree's "rights, powers and authority" and with the trust assets "which shall be held in trust for the benefit of claimants under this Plan." BCI was given the "exclusive authority to wind up the affairs of [Appletree] consistent with the terms of the Plan." The plan further "retain[ed] and preserve[d] all claims or interests belonging to [Appletree] or the estate" and authorized BCI "to pursue any claims and causes of action belonging to

[Appletree] against third parties, including * * * claims of malpractice[.]"

After commencing this legal malpractice action against O'Connor & Hannan, BCI moved to compel production of O'Connor & Hannan's files with respect to the federal action against W.R. Grace, a separate state case, and the Appletree bankruptcy case.[2] The motion was granted, but enforcement of the discovery order was stayed pending this appeal.

ISSUE

Did the district court err in denying O'Connor & Hannan's motion to dismiss this legal malpractice complaint?

ANALYSIS

[1,2] The question of a person's standing to bring suit is essential to a court's exercise of jurisdiction. *See Annandale Advocate v. City of Annandale*, 435 N.W.2d 24, 27 (Minn.1989). Whether a trial court has subject matter

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[2]O'Connor & Hannan also represented Appletree in a state suit initiated in Hennepin County against the building's original owner and architect, *Appletree v. Investmark, Inc.*, 91-16792, which was consolidated with another case entitled *New York Life Ins. Co. v. Landmark Dev. Corp.*, 91-19600. These cases, along with the federal case against W. R. Grace, were still pending when the creditors' plan was confirmed.

jurisdiction is a question of law which this court reviews de novo. *Cf. Ojala v. St. Louis County,* 522 N.W.2d 342, 343 (Minn.App.1994).

[3] The assignment of a legal malpractice claim is contrary to Minnesota public policy. *Wagner v. McDonald,* 509 N.W.2d 188, 193 (Minn.App.1993). Such an assignment would convert these claims into commodities "to be exploited and transferred to economic bidders who have never had a professional relationship with the attorney," thus making the assignment incompatible with the attorney's duty of confidentiality and detrimental to the unique and personal nature of the attorney-client relationship. *Id.* At 191 (quoting *Goodley v. Wank & Wank, Inc.,* 62 Cal.App.3d 389, 133 Cal.Rptr. 83, 87 (1976)).

This action vividly demonstrates these dangers. BCI's prosecution of this action threatens O'Connor & Hannan's duty of confidentiality to its former client. Indeed, Appletree's former general partners have objected to the release of any files and have indicated that they do not intend to waive or release any attorney-client privilege. And, by creating a liquidating plan with the express goal of removing control of the claim from Appletree, Appletree's creditors have essentially converted this malpractice claim into an economic asset or commodity.

[4] The prohibition against assignment of legal

malpractice claims is not altered by the fact that this case involves a bankruptcy debtor and a confirmed plan of liquidation expressly designed to transfer this malpractice claim to BCI. While the bankruptcy code permits the transfer of nonassignable claims into a bankruptcy estate by preemptive language, no similar preemptive language exists to permit the transfer of such claims of the estate. *See* 11 U.S.C. § 541(a)(1), (c)(a); *Pappas v. Sommer,* 240 Neb. 609, 483 N.W.2d 146, 148 (1992). Once otherwise nontransferable assets are acquired by a bankruptcy estate, those assets are subject to applicable nonbankruptcy laws. *Cf. In re Schauer,* 835 F.2d 1222, 1225 (8th Cir.1987) (consistent with state law, patronage margin certificates not transferrable or assignable from bankruptcy estate without approval of farm cooperative); *In re Farmers Markets, Inc.,* 792 F.2d 1400, 1402-03 (9th Cir.1986) (involving nontransferable liquor licenses). Thus, Minnesota law applies to the transfer or assignment of a legal malpractice claim out of a bankruptcy estate, and it prohibits such an assignment. *Cf. Picadilly, Inc. v. Raikos,* 582 N.E.2d 338, 339 (Ind.1991); *Earth Science Labs, Inc. v. Adkins & Wondra, P.C.,* 246 Neb. 798, 523 N.W.2d 254, 257 (1994) (public policy prohibits purchasing legal malpractice claim from bankruptcy estate from asserting claim); *Can Do, Inc. v. Manier, Herod, Hollabaugh & Smith,* 922 S.W.2d 865, 869 (Tenn.1996).

[5]This result is not changed by the appointment of a

representative under 11 U.S.C. § 1123(b)(3)(B) ("any claim or interest belonging to the debtor or to the estate" may be brought in post-confirmation action if reorganization plan provides for "retention and enforcement" of claim by representative of estate "appointed for that purpose"). *See also Harstad v. First Am. Bank,* 39 F.3d 898, 902-04 (8th Cir.1994). BCI cites a number of cases construing section 1123(b)(3)(B) that have allowed a representative to assert even nonassignable claims of a reorganized debtor. *See, e.g., In re Texas Gen. Petroleum Corp.,* 52 F.3d 1330, 1336 (5th Cir.1995) (liquidating trustee has standing to exercise fraudulent conveyance powers of debtor); *In re Sweetwater,* 884 F.2d 1323, 1327 (10th Cir.1989) (properly appointed trustee has standing to bring post-confirmation avoidance action). These cases, however, involve interests created or governed by federal bankruptcy law, not state law. These cases also tend to acknowledge that a "transfer" or "assignment" of claims to the representative has occurred. *See e.g., Texas Gen. Petroleum,* 52 F.3d at 1335. Thus, while the language of the liquidation plan specifically authorizes post-confirmation enforcement of the legal malpractice claim by BCI, this constitutes an impermissible and prohibited assignment under Minnesota law.

DECISION

The District court erred in denying O'Connor & Hannan's motion to dismiss the complaint.

Reversed.

John A. COCHRANE, Respondent (C8-94-1813), Appellant (C4-94-2036),

v.

TUDOR OAKS CONDOMINIUM PROJECT, an Ontario Limited Partnership, Nul Tiel, Respondent,

K.S.C.S. Properties, Inc., a Minnesota Corporation, Applicant for Intervention, Appellant (C8-94-1813).

Nos. C8-94-1813, C4-94-2036.

Court of Appeals of Minnesota.

March 28, 1995.

Review Denied May 31, 1995

Syllabus by the Court

A judgment debtor who has not previously raised the issue of a judgment creditor's capacity to sue has waived the right to do so, and may not seek to vacate the judgment on the grounds that the judgment creditor lacked capacity to sue.

Jan Stuurmanns, Law Offices of Jan Stuurmans, P.A., Minneapolis, for Cochrane.

Wood R. Foster, Jr., Jordan M. Lewis, Siegel, Brill, Greupner & Duffy, P.A., Minneapolis, for Tudor Oaks Condominium Project.

Laura J. Hanson, Joseph W.E. Schmitt, Meagher & Geer, Minneapolis, Thomas M. Zappia, Fridley, for K.S.C.S. Properties, Inc.

Considered and decided by HUSPENI, P.J., HARTEN and FOLEY*JJ.

OPINION

HUSPENI, Judge.

Following protracted litigation and an appeal in the underlying action, respondent Tudor Oaks Condominium Project was awarded a judgment against appellants John A. Cochrane and K.S.C.S. Properties. Appellants brought this action seeking to have the judgment vacated, alleging the judgment was void because it was obtained by a *nul tiel* entity. Tudor Oaks moved for summary judgment on the grounds that appellants had waived their right to challenge Tudor Oaks' status as a corporate entity by proceeding with the underlying action; the motion was granted. Appellants now seek to have the summary judgment reversed and to have this court remand with instructions to vacate the underlying judgment. Because we find that appellants have waived their right to challenge Tudor Oaks' capacity to sue, we affirm the grant of summary judgment.

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*Retired judge of the Minnesota Court of Appeal, serving by appointment pursuant to Minn. Const. Art. VI § 10.

FACTS

In 1987, S.B. McLaughlin & Co. (McLaughlin) brought an action against John Cochrane, K.S.C.S. Properties, Inc. (KSCS), Tudor Oaks Condominium Project (Tudor Oaks), and ABIO Holdings, Inc. (ABIO). McLaughlin proceeded as plaintiff individually and in a derivative capacity on behalf of Tudor Oaks and ABIO, alleging that Cochrane and KSCS had breached their fiduciary duties. When suit was commenced, Tudor Oaks was a limited partnership chartered in Ontario, Canada. ABIO, Tudor Oaks's general partner, was a Minnesota corporation. McLaughlin was a limited partner of Tudor Oaks.

The action was removed to federal court on diversity of grounds. On September 12, 1989, McLaughlin acquired sole ownership of Tudor Oaks and ABIO. On August 19, 1990, Tudor Oaks lost its limited partnership charter in Ontario. The action was remanded to the state district court in November 1990. On October 11, 1991, ABIO was statutorily dissolved in Minnesota.

On December 12, 1991, McLaughlin moved to amend its complaint to reflect its sole ownership of Tudor Oaks and ABIO. The district court granted McLaughlin's motion on January 10, 1992. This eliminated McLaughlin's derivative action against Tudor Oaks and ABIO, and realigned Tudor Oaks and ABIO as plaintiffs proceeding in their own right against Cochrane and KSCS. The parties did not inform the court that Tudor Oaks had dissolved or that ABIO was no

longer a legal entity.

The case proceeded to trial in the summer of 1992. The jury returned a special verdict finding Cochrane had breached a fiduciary duty to McLaughlin, causing damages of $792,000. The jury also found Cochrane had breached a fiduciary duty to Tudor Oaks, causing damages of $1.628 million, and that KSCS had conspired with Cochrane to breach a fiduciary duty to Tudor Oaks, causing damages of $3.52 million.

On appeal, this court reversed the award to McLaughlin, holding that as a matter of law Chochrane owed no fiduciary duty to McLaughlin. *See S.B. Mclaughlin & Co., Ltd. V. Cochrane,* No. C4-92-2081, 1993 WL 231672 (Minn.App. June 29, 1993), *pet. For rev. denied* (Minn.Aug.24, 1993). This court also reduced the remaining damages owed by KSCS and Cochrane to $1.26 million. *Id.*

In late 1993 and early 1994, Cochrane and KSCS brought actions to obtain relief from the judgment, arguing that the dissolution of Tudor Oaks and ABIO deprived the district court of subject matter jurisdiction, and that the judgment had been procured by fraud. Both actions were consolidated and Tudor Oaks moved for judgment on the pleadings. Tudor Oaks conceded that its limited partnership registration had expired and that ABIO, its general partner, was dissolved. The district court held genuine issues of fact exist regarding whether the judgment was procured by fraud, but ordered summary judgment of Tudor Oaks, holding that

the fraud issue should have been raised during the previous trial. The court also held that even though Tudor Oaks did not have a right to maintain an action as a dissolved partnership, Canadian law allowed McLaughlin, as the only remaining partner, to continue the action because it was commenced before the partnership dissolved. This appeal followed.

ISSUES

1. Are subject matter jurisdiction and standing viable theories of this case?

2. Did appellants waive their right to challenge Tudor Oaks' capacity to sue by not timely challenging it?

ANALYSIS

[1] Tudor Oaks moved for judgment on the pleadings under Minn.R.Civ.P. 12.03. Because appellants presented matters outside the pleadings, Tudor Oaks' request for dismissal was treated as a motion for summary judgment. *See* Minn.R.Civ.P. 12.02.

> On appeal from a summary judgment, this court must determine (1) whether there are any genuine issues of material fact, and (2) whether the trial court erred in its application of the law.

City of Virginia v. Northland Office Properties, 465 N.W.2d 424, 427 (Minn.App.1991), *pet for rev. denied* (Minn. April.

18, 1991). Even though an appellate court may disagree with the trial court's analysis, summary judgment will be affirmed if it can be sustained on any grounds. *Myers v. Price,* 463 N.W.2d 773, 775 (Minn.App. 1990), *pet for rev. denied* (Minn. Feb. 4, 1991).

[2] Appellants argue the district court erred in its conclusion that the question of fraud should have been raised in the underlying action. "On appeal, this court need not defer to the trial court's conclusion when reviewing questions of law." *County of Lake v. Courtney,* 451 N.W.2d 338,340 (Minn.App.1990), *pet. For rev. denied* (Minn. Apr. 13, 1990).

1. Appellants frame their argument in terms of "standing" and "subject matter jurisdiction." We believe, however, that neither theory is applicable to the case at hand. Rather, we conclude that the issue we must address is more properly analyzed in terms of "capacity to sue." A brief discussion of the differences among these three concepts may aid our resolution of the question raised by the case.

[3] Subject matter jurisdiction has been defined as

> not only authority to hear and determine a particular class of actions, but authority to hear and determine the particular questions the court assumes to decide.

Duenow v. Lindeman, 223 Minn. 505, 511, 27 N.W.2d 421, 425 (Minn.1947) (quoting *Sache v. Wallace,* 101 Minn. 169,

172, 112 N.W. 386, 387 (Minn.1907)). Because subject matter jurisdiction goes to the authority of the court to hear a particular class of actions, lack of subject matter jurisdiction may be raised at any time, including for the first time on appeal. Minn.R.Civ.P. 12.08(c) ("[w]henever it appears* * * that the court lacks jurisdiction of the subject matter, the court shall dismiss the action"); *Berke v. Resolution Trust Corp.*, 483 N.W.2d 712, 714 (Minn.App.1922) (claimed lack of subject matter jurisdiction raised for the first time on appeal), *pet. for rev. denied* (Minn. May 21, 1992).

Despite the fact that appellants couch certain of their arguments on appeal in terms of subject matter jurisdiction, there is no question that the district courts of Minnesota have jurisdiction to consider matters brought under Minn.R.Civ.P. 60.02 or any other Minnesota Rule of Civil Procedure, to consider matters brought under Minn.Stat. § 548.14 (1992) and to consider any of the legal or equitable theories raised in a case. Nor is there any claim that the district court here violated the ruling set forth in *Duenow*, 223 Minn. 505, 27 N.W.2d 421[1] Any relief granted to appellants must be granted under a theory other than that of lack of subject

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[1]In *Duenow*, the trial court granted default judgment beyond the "issues made by the pleadings." 223 Minn. at 511, 27 N.W. 2d at 425. The Supreme Court, in vacating the default judgment and reversing to permit defendants to answer, stated that "relief which may be awarded against a defendant who does not answer must be limited in kind and degree to that specifically demanded in the complaint." *Id.*

matter jurisdiction.

[4] We are also unable to bring appellants' challenges within the concept of "standing." This court has observed that "standing has been called one of the most amorphous concepts in the entire domain of public law." *Sundberg v. Abbott,* 423 N.W.2d 686, 688 (Minn.App.1988) (citation omitted), *pet. for rev. denied* (Minn. June 29, 1988).

> The concept of standing is filled with complexities and uncertainties [,but] the fundamental aspect of standing is that it focuses on the party seeking to get his complaint before a court and not on the issues he wishes to have adjudicated.

Id. (Citations and quotations omitted). Essentially, a potential litigant must allege injury in fact, or otherwise have a sufficient stake in the outcome, to have a court decide the merits of a dispute. *See Middlewest Motor Freight Bureau v. United States,* 525 F.2d 681, 683 (ith Cir.1975) (discussing federal requirement of standing).

[5] Standing may be raised at any time. *In re Welfare of Mullins,* 298 N.W.2d 56, 61 n. 7 (Minn.1980). Nonetheless, courts appear hesitant to deny standing under circumstances which would prejudice the party whose standing would be found lacking. The eighth circuit in *Middlewest,* having noted that satisfaction of the constitutional element of

standing requires that a plaintiff allege a sufficient stake in the outcome of the litigation, denied a challenge to standing. 525 F.2d at 683.

> Policy factors in the instant case favor the conclusion that the appellants have the requite standing. Appellants have been litigating the merits of the controversy for approximately ten years without anyone challenging their standing to do so. Moreover, a denial of standing* * * at this time would [be] unduly prejudic[ial].

Id.

We find no basis upon which to apply the doctrine of standing. McLaughlin (originally the sole plaintiff in the 1987 action) clearly had a stake in the outcome of that litigation. Tudor Oaks and ABIO were originally defendants in that action.

[6] 2. In contrast to subject matter jurisdiction, which concerns the court's ability to consider a question, and standing, which concerns a party's right to bring a particular action, capacity to sue concerns a party's right to maintain any action. By arguing that Tudor Oaks did not have the right to maintain an action, appellants are in fact arguing Tudor Oaks' lack of capacity to sue. *See Lehigh Valley Coal Co. V. Gilmore,* 93 Minn. 432, 434, 101 N.W. 796 797 (Minn.1904) (objection to a foreign corporation's failure to show compliance with statutes goes to the corporation's right to maintain an action).

Appellants base their argument on Minn.Stat. § 322

A.75(a) (1992):

> A foreign limited partnership transacting business in this state may not maintain any action, suit, or proceeding in any court of this state until it has registered in this state.

Because Tudor Oaks had not complied with the registration requirements, appellants argue hat it had no capacity to maintain an action, and that the judgment issued in Tudor Oaks' favor should therefore be vacated.[2]

[7, 8] However, capacity to sue differs from both subject matter jurisdiction and standing in another very material way. While both subject matter jurisdiction and standing may be challenged at any time, the right to challenge capacity to sue is waived if it is not timely asserted. *See Risvold v. Gustafson,* 209 Minn. 357, 296 N.W. 411 (Minn.1941) (the issue of the corporation's right to sue should have been pleaded); *Lehigh Valley,* 93 Minn. at 434, 101 N.W. at 797 (objection to plaintiff's ability to maintain the action where want of capacity does not appear on the face of the complaint,

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[2]We note that prior to its acquisition by the then sole plaintiff, S.B. McLaughlin, Tudor Oaks was not maintaining an action as "maintaining" has been defined by the Supreme Court. "To 'maintain' an action is to uphold, continue on foot, and keep from collapse a suit already begun, or to prosecute a suit with effect. *George Moore Ice Cream Co. v. Rose, Ga.* 289 U.S. 373 [53 S.Ct. 620, 77 L.Ed. 1265 (1933)]." Black's Law Dictionary 859 (5th ed. 1979).

could only be raised by answer). By failing to object prior to trial to Tudor Oak's incapacity to sue by virtue of its defective registration, appellants waived their right to so object.

Risvold, like the case her, concerned a foreign corporation not licensed to do business in the state. A shareholder, respondent on appeal, had brought an action on behalf of the corporation.

> [A]t the trial, appellants moved to dismiss, arguing that inasmuch as the corporation could not have maintained the action, plaintiff was not entitled to sue on its behalf. That point was not made by answer or otherwise before the motion to dismiss. It was then too late. The issue is one of the corporation's right to sue. In order to be of avail to [appellants], it should have been pleaded.

Id. 209 Minn. at 361, 296 N.W. ar 413. *Lehigh Valley* likewise involved an action brought by a foreign corporation; while the corporation alleged in the complaint that it was lawfully doing business in Minnesota, it did not show any proof of compliance with the statutes governing foreign corporations. 93 Minn. at 432, 101 N.W. at 796.

> [F]or this reason defendants urge that no recovery can be had by it. We do not concur in this contention.* * * [D]efendants did not answer, or at any time during the trial make the point, that [the corporation] had failed to show a compliance with the statues.* * * It was clearly incumbent upon defendants affirmatively to allege in their answer a failure on the part of plaintiff to comply with the statutes on this subject, and having failed to do so, the defense is no available

to them.

Id. at 434, 101 N.W. at 796. Challenges to a foreign corporation's right to maintain an action are clearly challenges to its capacity to sue, not to its standing, nor to the court's subject matter jurisdiction. As such, they must be timely raised.

This requirement is supported by longstanding case law concerning incapacity to sue in a variety of contexts. *Brazney v. Barnard,* 169 Minn. 501, 211 N.W. 949 (Minn.1927) held that a party could not challenge a verdict on the grounds that the other party

> is insane, and therefore is without legal capacity to sue. * * * If such defect appeared from the complaint, it should have been taken advantage of by demurrer, otherwise by answer. Not having been taken advantage of by either demurrer or answer, it is deemed to have been waived.

Id. at 503, 211 N.W. at 950.[3] *Dalsgard v. Meierding,* 140 Minn. 388, 168 N.W. 584 (Minn.1918) also found a defendant to have waived the right to challenge the capacity to sue of the plaintiff, an infant, holding that

> the defendant, by answering to the merits, had waived

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[3]Minn.R.Civ.P. 7.01 terminated the use of demurrers by providing for pleading only by complaint and answer. However "[a]n examination of the advisory committee's notes on Rule 7.01* * * indicates that the primary purpose of abolishing demurrers* * * was essentially one to effect a change of terminology or form and not of function." *House v. Hanson,* 245 Minn. 466, 468, 72 N.W.2d 874, 875 (Minn.1955).

> the objection that there was a want of capacity in the plaintiff to sue.* * * [W]here there is a want of capacity to sue appearing affirmatively upon the face of the complaint, the defendant may demur thereto.* * * [O]bjections not so taken by demurrer shall be deemed waived.

Id. at 390-91, 168 N.W. at 585. *Miller v. Maier,* 136 Minn. 231, 161 N.W. 513 (Minn.1917) found a party to have waived the right to challenge the voting status of contestants of an election.

> It is not sufficient after the trial and decision for contestee to say that it does not appear that contestants had the capacity to sue, or its equivalent, to bring this contest. If contestee wished to raise this question, he should have done so by demurrer or answer, otherwise he is deemed to have waived the same.

Id. at 235, 161 N.W. at 515. Similarly, *Lee v. Scriver,* 143 Minn. 17, 172 N.W. 802 (Minn.1919) rejected a challenge based on the incapacity to sue of two estates named as plaintiffs.

> If the decedents had an interest in the cause of action and their successors in interest have not been made parties, this at most would only amount to a defect of parties, and such defect has been waived by failing to point it out.

Id. at 20, 172 N.W. at 803. Challenge to capacity to sue arising from whatever cause, must be asserted long before it was asserted here.

Nor is capacity to sue unique; an objection to *any*

defect in parties must be timely raised. *See, e.g., Flowers v. German,* 211 Minn. 412, 420, 1 N.W. 2d 424, 428 (Minn.1941) ("If no such objection is made the defect will be deemed waived. And there is no distinction as to such defect between parties plaintiff and defendant"); *Bell v. Mendenhall,* 71 Minn. 331, 336, 73 N.W. 1086, 1088 (1898) (Where a party elects to proceed with an action without the proper parties before the court, any objection to the parties is deemed waived).

The Minnesota Supreme Court has repeatedly asserted that objections to parties cannot be deferred.

> Under our practice, if there be defect of parties, whether plaintiff or defendant, and * * * no such objection is taken advantage of either by demurrer or answer, defendant is deemed to have waived the same. He cannot later raise the objection by motion for dismissal, for judgment on the pleadings, for direction of verdict, or by objection to the evidence.* * * Here no such preliminary steps were taken. The case was tried on this merits and disposed of upon the issues presented by the pleadings.

Serr v. Biwabik Concret Aggregate Co., 202 Minn. 165, 183, 278 N.W. 355, 365 (Minn.1938). Reargument was therefore denied. *Id.* Where defect was raised not in the pleadings but during trial by a motion to dismiss and a motion to amend the answer, the denial of these motions was upheld. *Hanson v. Bowman,* 199 Minn. 70, 74-75, 271 N.W. 127, 129 (Minn.1937).

[C]onsidering that the case was half tried before there

> was any attempt to plead defect of parties, * * * we think there was no abuse of discretion in denying the amendment asked.

Id. The Minnesota Supreme Court has denied rehearing where

> [t]he defect of parties was clearly waived by defendant. At no time during the trial of the action was the point called to the attention of the trial court, except at the close of the evidence, and then only by a request for an instructed verdict in defendant's favor.

Mason v. St. Paul Fire & Marine Ins. Co., 82 Minn. 336, 341, 85 N.W. 13, 15 (Minn.1901).

Finally, in a case with a time frame similar to that here, the eighth circuit held that the right to object to a defect in parties plaintiff was waived "unless the issue is promptly raised." *Capital Fire Ins. Co. Of California v. Langhorne,* 146 F.2d 237, 243 (8th Cir. 1945).

> When the present action was begun the appellant made no objection that there was a defect of parties plaintiff. * * * Approximately two years elapsed between the institution of appellee's action and the date of its trial. During this time the appellant never raised the objection based upon a defect of parties. * * * The issue of a defect of parties plaintiff was put into the case at the beginning of this trial.

Id. at 242-43. The defendant was found to have waived the right tot challenge a defect in parties by failing to raise it prior to trial.

Here, the district court concluded that Tudor Oaks is

entitled to summary judgment as a matter of law because appellants failed to challenge its capacity to sue before trial, during the trial, or at any time prior to the post-appeal entry of judgment. The district court noted that the circumstances giving rise to Tudor Oaks' alleged incapacity to sue were a matter of public record throughout the first trial; therefore, appellants could unquestionably have substantiated a challenge to Tudor Oaks' capacity to sue.

The district court pursued an analysis of Minn.Stat § 548.14 to reach its conclusion that appellants' failure to timely challenge Tudor Oaks' right to maintain an action cannot be excused by fraud, because the information allegedly fraudulently concealed from appellants was in fact available to them as a matter of public record. Without resorting to the statute, we reach the identical conclusions: appellants' failure to timely challenge Tudor Oaks' right to maintain an action was in fact a failure to timely challenge its capacity to sue, and waived appellants' right to assert the challenge.

Appellants argue that *Halloran v. Blue & White Liberty Cab Co.*, 253 Minn. 436, 92 N.W.2d 794 (Minn.1958) mandates remanding this case to the district court with instructions to vacate the underlying judgment.[4] *Halloran* was an appeal from the denial of a motion to amend a

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[4]This is the sole relief ever requested by appellant KSCS and the sole relief requested in the conclusion to his brief by appellant Cochrane, although at one point in the brief he requests "at a minimum" remanding for further findings.

judgment obtained against a nonexistent corporation, brought by the judgment creditors after they had first made two unsuccessful attempts to bring an action against the real defendants. The Minnesota Supreme Court remanded for further findings as to whether the real defendants, their insurers and their attorneys had intentionally deceived or misled the court, after noting that any such intentional deception as to the true identity of a litigant would constitute a fraud upon the court. *Id.* At 443, 92 N.W.2d at 798-99.

We find that appellants' reliance on *Halloran* is misplaced, since there are critical distinctions between this case and *Halloran.* First, by asking this court to remand with instructions to vacate, appellants seek far more than the supreme court granted in *Halloran.* There, even though there was no question that the defendant named in the judgment did not exist, the supreme court did not permit amendment of the judgment with the names of the real defendants; it remanded for further findings. By remanding with instructions to vacate the underlying judgment, as appellants would have us do, we would in effect nullify the results of some eight years of litigation on the basis of one alleged deception, although the true facts were readily available. Secondly, the appellants in *Halloran* asked an appellate court to rectify a defect in parties in order to give effect to trial court judgment; appellants here ask this court to use a defect in parties as a basis for setting aside a district court judgment. Finally, the identity question in *Halloran* concerned a party who was a defendant

throughout, from whom recovery was sought and obtained, so the issue of that party's capacity to sue never arose; here, the identity question was raised to challenge the capacity to sue of a party variously denominated as both plaintiff and defendant, and now entitled to recover.

We would note that it is the entitlement to recovery, not the actual capacity to recover by enforcing the judgment, which is the issue here. Like the panel of this court which decided the previous appeal in this matter, we do not reach the issue of who will enforce this judgment or how it will be enforced. *See McLaughlin,* unpub. Op. At 9 n. 3.

Finally, because we affirm the award of summary judgment for Tudor Oaks and because Tudor Oaks did not file a notice of review, we do not address Tudor Oaks' allegation that the district court erred in determining that appellants could bring claims pursuant to Minn.Stat. § 548.14 and Minn.R.Civ.P. 60.02 in the same action.

DECISION

Appellants, by failing to challenge Tudor Oaks' capacity to sue throughout protracted litigation until after the final entry of judgment, waived their right to that challenge. Tudor Oaks is entitled to summary judgment dismissing appellants' motion to vacate.

Affirmed.

DANIEL F. FOLEY, Judge (dissenting).

I respectfully dissent, and would reverse and remand

to the trial court to vacate the judgment that was entered in favor of Tudor Oaks, a non-entity.

This action was commenced by S.B. McLaughlin in June 1987. At that time, Tudor Oaks, a limited partnership, and ABIO, Tudor Oaks' general partner, were named as defendants, along with Cochrane and KSCS. In September 1989, however, S.B. McLaughlin became the sole limited partner of Tudor Oaks and the sole shareholder of ABIO. On January 10, 1992, Tudor Oaks and ABIO were realigned with S.B. McLaughlin as plaintiffs in S.B. McLaughlin's action against Cochrane and KSCS.

At the commencement of the action in June 1987, Tudor Oaks was an Ontario limited partnership, and ABIO, Tudor Oaks' general partner, was a Minnesota corporation. Before the realignment of the parties occurred in January 1992, however, Tudor Oaks' status as an Ontario limited partnership was dissolved. Furthermore, on October 11, 1991, ABIO's status as a Minnesota corporation was dissolved. No effort was made to continue ABIO in existence under Minnesota law. According to Ontario law, the dissolution of a corporate general partner automatically dissolves a limited partnership unless the partnership is continued by the remaining general partners pursuant to the partnership agreement or by consent. Ontario Limited Partnerships Act, 6 R.S.O., ch. L. 16 § 21 (1990). Because there was no such provision in Tudor Oaks' partnership agreement and because there were no remaining general

partners, effective October 1991, Tudor Oaks' status as a limited partnership ceased.

Therefore, at the time of realignment of the parties in January 1992, Tudor Oaks was a nonexistence limited partnership--a nonentity. As I view the record, no one seriously disputes the fact that Tudor Oaks is a phantom judgment creditor, now and when judgment was entered in its favor.

At the time the pleadings were amended and the parties realigned, the complaint realleged the existence of Tudor Oaks and ABIO as legal entities. However, the undisputed fact is that the complaint was pursued by Tudor Oaks and ABIO, who were actually nonexistent plaintiffs. A suit that is brought in the name of that which is not a legal entity is a mere nullity. *J.C. Peacock, Inc. v. Hasko,* 184 Cal.App.2d 142, 7 Cal.Rptr. 490, 496 (1960). A plaintiff who is not a legal entity is without legal capacity to sue. *Id.; Robertson v. Brown,* 75 N.D. 109, 25 N.W. 2d 781, 784 (N.D. 1947); *Philadelphia Facilities Management Corp. v. Biester,* 60 Pa.Cmwlth. 366, 431 A.2d 1123, 1127 (1981); *see St. Paul Typothetae v. St. Paul Bookbinders' Union No. 37,* 94 Minn. 351, 357, 102 N.W. 725, 726 (1905) (to be entitled to sue, a party must be a natural or an artificial person).

Minnesota law provides that a foreign limited partnership may not sue in this state until it has registered in the state. Minn. Stat. § 322A.75(a) (1992); *see also* Minn.Stat. § 322A.73 (1992) (Foreign limited partnership

must correct registration application when any facts change). At the time Tudor Oaks was realigned in this action as a plaintiff, it could not have been properly registered in this state because it was a nonexistent entity.

The trial court placed on Cochrane and KSCS the burden of proving the nonexistence of Tudor Oaks limited partnership. The court concluded that the failure of Cochrane and KSCS to timely raise the issue of capacity to sue must permit the judgment to stand.[1] But the interesting inquiry then follows: How does a phantom creditor enforce its judgment?

The trial court originally entered judgment in favor of S.B. McLaughlin and Tudor Oaks. Judgment was entered in favor of Tudor Oaks on September 24, 1992 in the sum of $1.628 million, later modified as to amount by this court. On appeal, this court reversed the portion of the judgment in favor of S.B. McLaughlin--this court reasoned that no fiduciary relationship existed between Cochrane and S.B. McLaughlin to support a judgment in S.B. McLaughlin's favor. Therefore, the only judgment remaining in this action is in favor of Tudor Oaks, modified by this court in a prior

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[1]Although capacity ordinarily should be raised by specific negative averment, capacity to sue was not an issue at the time of the original complaint by S.B. McLaughlin. At the time of the original complaint, Tudor Oaks and ABIO were defendants, rather than plaintiffs. Furthermore, at that time neither Tudor Oaks nor ABIO had been dissolved. Once they were dissolved, they ceased to exist as legal entities.

appeal. The court has inherent power to vacate a judgment that is a nullity; a void judgment may be vacated anytime. *Peterson v. Eishen,* 512 N.W. 2d 338, 341 (Minn.1994); *accord Simonds v. Norwich Union Indem. Co.,* 73 F.2d 412, 415 (8th Cir.1934), *cert. denied,* 294 U.S. 711,55 S.Ct. 507, 79 L.Ed. 1246 (1935).

The cases cited by the majority are distinguishable, since they involve entities or individuals that actually exist. Here, it is conceded that when judgment was entered in this favor, Tudor Oaks was a nonexistent entity. Because the judgment has been entered in favor of a nonexistent entity, the possibility of enforcement of the judgment has been entered in favor of a nonexistent entity, the possibility of enforcement of the judgment is equally nonexistent, and the judgment should be discharged of record. The judgment in favor of Tudor Oaks is a void judgment and "cannot gain validity by the passage of time." *Eishen,* 512 N.W.2d at 341.

STATE OF MINNESOTA DISTRICT COURT

COUNTY OF
HENNEPIN FOURTH JUDICIAL DISTRICT

John A. Cochrane,

Plaintiff,

vs. ORDER

File No. 93-16553

Tudor Oaks Condominium Project,
an Ontario Limited Partnership, Nul Tiel,

Defendant.

K.S.C.S. Properties, Inc.,
A Minnesota corporation,

Plaintiff,

vs.

Tudor Oaks Condominium Project,
an Ontario Limited Partnership, Nul Tiel,

Defendant.

The above-entitled matter came on for Hearing before the Honorable Gary Larson on June 1, 1994 upon a motion for summary judgment filed by the Defendant.

Jan Stuurmans, Esq., Suite 600, 400 Second Avenue South, Minneapolis, Minnesota 55401, appeared for and on behalf of Plaintiff, John A. Cochrane.

Thomas M. Zappia, Esq., 941 Hillwind Road

Northeast, Suite 301, Fridley, Minnesota 55432, appeared for and on behalf of KSCS Properties, Inc., a Minnesota corporation.

Wood R. Foster, Esq., and Jordon Lewis, Esq., 1300 Washington Square, 100 Washington Avenue South, Minneapolis, Minnesota 55402, appeared for and on behalf of Defendant, Tudor Oaks Condominium Project, an Ontario Limited Partnership, Nul Tiel.

Now, therefore, based upon all the files, records and proceedings herein:

THE COURT HEREBY ORDERS:

1. That Defendant's motion for summary judgment shall and is hereby, in all respects GRANTED;

2. That the Court Administrator is hereby ordered to enter summary judgment in favor of Defendant and against Plaintiffs, together with Defendant's taxable costs and disbursements.

LET JUDGMENT BE ENTERED ACCORDINGLY

Dated:
7/6/94

BY THE COURT:
/s/ Gary Larson
Gary Larson
Judge of the District Court

MEMORANDUM

I. FACTS

Plaintiffs are bringing this cause of action under Minn.Stat.§ 548.14 and pursuant to Minn.R.Civ.Pro. 60.02. Plaintiffs, allege that the judgment against them, entered by the District Court of Hennepin County, on September 25, 1992, should be vacated. Plaintiffs claim that the judgment is void because it was obtained by a nul tiel entity. Defendant Tudor Oaks Condominium Project (hereinafter "Tudor Oaks") has moved the Court for Summary Judgment.

For purposes of summary judgment, all doubts and factual inferences must be resolved against the moving party and in favor of the nonmoving party. Nord v. Herreid, 305 N.W.2d 337, 339 (Minn. 1981); See Dempsey v. Jaroscak, 168 N.W.2d 779, 781-82 (Minn. 1971).

This action stems from a 1987 lawsuit, in which S.B. McLaughlin & Company brought an action in Hennepin County District Court against Tudor Oaks Condominium Limited Partnership, ABIO Holdings Inc., John A. Cochrane, K.S.C.S. Properties Inc. And John Does. Plaintiff in that action alleged a breach of fiduciary duty directly and derivatively against John Cochrane and KSCS. Plaintiff sought derivative relief on behalf of Tudor Oaks and its general partner, ABIO. The action was originally removed to the United States District Court for the District of Minnesota, where it remained until it was remanded to Hennepin County District Court in November of 1990. It should be noted that

Cochrane sought to have the case heard in State Court, opposing venue in Federal Court.

On December 12, 1991 S.B. McLaughlin moved the State Court to realign the parties based on the fact the S.B. McLaughlin had acquired the remaining interest in Tudor Oaks and ABIO. Chochrane represented Tudor Oaks and ABIO at the time S.B. McLaughlin acquired this interest. The result of the realignment was that the derivative claims against Tudor Oaks and ABIO were dismissed.

On September 22, 1992, the trial court entered an Amended Order for Judgment. The Court of Appeals modified the judgment in favor of Tudor Oaks on June 22, 1993 and the Minnesota Supreme Court denied a petition for review on August 24, 1993.

Cochrane and KSCS bring this action to vacate the judgment in the previous case based on the fact that Tudor Oaks and ABIO were not in good standing at the time judgment was entered by the District Court. Plaintiffs allege that Tudor Oaks and ABIO failed to maintain the limited partnership and corporate filings as required by Ontario and Minnesota law. Plaintiffs in this matter asserts that the judgment should be vacated because S.B. McLaughlin failed to disclose the fact that Tudor Oaks and ABIO were defunct. Also, Plaintiffs assert that the judgment in the previous action should be vacated based on the fact that McLaughlin concealed its purchase of all of the interest in Tudor Oaks. Plaintiffs argue that had that fact not been concealed diversity

of citizenship would not have been defeated and the case would have remained in Federal Court.

II. Summary Judgment

Under the Minnesota Rules of Civil Procedure, a grant of summary judgment is proper when:

> the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no issue as to any material fact and that either party is entitled to judgment as a matter of law.

Minn. R. C.V. P. 56.03. "Summary judgment is not a substitute for trial and may be granted only if, based on the entire record, no material fact exists, and the moving party is entitled to judgment as a matter of law." Biller v. J.C.D. Penney Co., Inc., 376 N.W.2d 209, 215 (Minn. 1985). A material issue of fact is one which would affect the outcome of the case. Pischke v. Kellen, 348 N.W. 2d 201, 205 (Minn. Ct. App. 1986) (citing Rathbun v. W.T. Grant Co., 219 N.W.2d 641, 646 (Minn. 1974)).

Summary judgment has been characterized as a "blunt instrument" which "should be employed only where it is perfectly clear that no issue of fact is involved in the cause of action." Donnay v. Boulware, 144 N.W.2d 711, 716 (Minn. 1966). The Minnesota Supreme Court has stated that the "burden is on the moving party to show the absence of any material fact." Biller, 376 N.W.2d at 215 (citing Barilla v. Clapshaw, 237 N.W.2d 830, 831 (Minn. 1976)); See Thiele

v. Stich, 425 N.W.2d 580, 583 (Minn. 1988) (the burden is on movant to establish that no genuine issue of material fact exists). When determining whether the moving party has sustained its burden, the court must view the evidence in a manner most favorable to the nonmoving party. See Sauter v. Sauter, 70 N.W. 2d 351, 353 (Minn. 1955); Ritter v. M.A. Mortenson Co., 352 N.W.2d 110, 112 (Minn. Ct. App. 1984) (citing Greaton v. Enich, 185 N.W.2d 876, 878 (Minn. 1971)). All doubts and factual inferences must be resolved against the moving party. Nord v. Herreid, 305 N.W.2d 337, 339 (Minn. 1981); See Dempsey v. Jaroscak, 188 N.W.2d 779, 781-82 (Minn. 1971).

It is only when the movant has satisfied its burden must the nonmoving party then show the existence of a genuine issue of material fact. Biller, 376 N.W.2d at 215 (citing Continental Sales and Equipment Co. v. Town of Stuntz, 257 N.W.2d 546, 550 (Minn. 1977)). If the nonmoving party ultimately fails to present specific facts indicating that a genuine issue of material fact exists, summary judgment is proper. Hunt v. IBM Mid Am. Employees Fed. Credit Union, 384 N.W.2d, 353, 355 (Minn. 1986). In order to successfully oppose a motion for summary judgment, the nonmoving party cannot rely upon mere averments or denials set forth in its pleadings, but must present specific facts showing that there is a genuine issue for trial. Minn. R. C.V.. P. 56.05; See Hunt v. IBM Mid Am. Employees Fed. Credit Union, 384 N.W.2d 353, 355 (Minn. 1986) (the nonmoving party cannot rely on mere general

statements of fact). Moreover, the court is not required to "rescue the nonmoving party from summary judgment by drawing unreasonable inferences." City of Savage v. Varey, 358 N.W.2d 192, 105 (Minn. Ct. App. 1984).

ANALYSIS

A. Claims Under Minn.R.Civ.Pro. 60.02 Are Not Improperly Pled Nor Are They Time-Barred.

Minnesota Rules of Civil Procedure allow a court to relieve a party from a final judgment on a motion and upon such terms as are just. Defendant argues that Plaintiffs have improperly pled Rule 60.02 because the rule does not allow for a new action but merely permits a motion to be brought. However, Rule 60.02 does not limit the power of a Court to entertain an independent action to relieve a party from a judgment and Rule 8.01 of the Minnesota Rules of Civil Procedure permits a Plaintiff to join different or alternative claims for relief in one pleading. Furthermore, the new action is brought before the original trial court, therefore, the Rule 60.02 motion is proper.

Defendant also argues that Rule 60.02 is time-barred because it was not brought within one year after judgment. Defendant states that Cochrane did not complete service in this matter until December 3, 1993.

Rule 60.02 authorizes two separate time periods within which a motion to vacate must be filed. "The motion shall be made within a reasonable time, and for reasons (a), (b), and © not more than 1 year after the judgment, order or

proceeding was entered or taken." Defendant argues that because the trial court entered judgment on September 25, 1992 and service in this matter was not complete until December 3, 1993, the Plaintiffs' claims, at least under Rule 60.02 (a) and (c), are barred by the one year time limit.

However, Defendant failed to address the fact that the judgment was appealed. An appeal suspends a judgment and deprives it of its finality until the appellate court has pronounced its decision or the appeal is dismissed. Holden v. M.A.C., 250 Minn. 130, 84 N.W.2d 282, 287 (1957). The judgment in the first case was appealed. It was not until August 24, 1993 that the Minnesota Supreme Court denied further review. Therefore, the judgment in the first matter was not final until August 24, 1993. The December 3, 1993, service of the Summons and Complaint in this present action was well within the one year deadline required by Rules 60.02 (a) and (c).

Plaintiffs have also brought motions under Rule 60.02 (d) and (f). These motions must be brought within a "reasonable time". However, subdivision (f) has been designated as a residual clause designed only to afford relief in those circumstances exclusive of the specific areas addressed by clause (a) through (e). See Simons v. Schiek's Inc., 275 Minn. 132, 138, 145 N.W.2d 548, 552 (1966). In this case, Plaintiffs have raised claims addressed by clause (a) through (e) of Rule 60.02. Therefore, this is not a situation where claims under Rule 60.02 (f) are appropriate.

B. There Are Genuine Issues of Fact As To Whether The Claims Brought Under Minnesota Statute § 548.14 Are Time-Barred.

Under Minnesota Statute § 548.14,

> "[a]ny judgment obtained in a court of record by means of perjury, subornation of perjury, or any fraudulent act, practice, or representation of the prevailing party, may be set aside in an action brought for that purpose by the aggrieved party in the same judicial district within three years after the discovery by the aggrieved party of such perjury or fraud."

Defendant argues that Plaintiffs are time-barred from raising a claim under Minn.Stat. § 548.14. Defendants argue that Cochrane must have known about the transferring of interest from Tudor Oaks and ABIO to S.B. McLaughlin, because the "Memorandum of Understanding" was dated September 12, 1989 and Cochrane was representing Tudor Oaks and ABIO at that time. It is Defendant's position that because those entities were Cochrane's clients, he must have had knowledge of the sale of their interest. Also, Defendant cites to a memorandum written by Cochrane dated September 25, 1990 which raises the possibility of a realigned party situation. Therefore, Defendant concludes that Cochrane must have known of the transferred interests at least by September 25, 1990. Because service was not complete by September 25, 1993, three years after Defendant argues that Cochrane knew about the alleged "fraud", claims under

Minn.Stat. § 548.14 would be barred.

However, the issues raised by Defendant address when Cochrane knew about the sale of interest in Tudor Oaks and ABIO. This is an issue of fact, not an issue of law. Therefore, the issue is not appropriate for summary judgment. The Court is unwilling to find that Plaintiffs' claims of fraud are time-barred based on Defendant's argument that Cochrane must have known about the realignment three years prior to this suit. If the Court were to make this determination it would be making findings of fact and this is not the proper role of the Court on a motion for summary judgment.

Also, Plaintiffs assert that they had no knowledge that the partnerships of Tudor oaks and ABIO had cease to exist until January or February, 1993. Therefore, there is a material issue of fact as to whether Plaintiffs discovery of the alleged fraud in that case was within the three year time limitation set forth in Minn.Stat. § 548.14.

C. As A Matter Of Law, The Defendant Is Entitled to Summary Judgment Under Minn.Stat. § 548.14 Because Plaintiffs' Defense Should Have Been Raised During The Previous Trial.

An Action or motion to vacate a judgment for fraud is extraordinary and should only be allowed in unequivocal cases. Minn.Stat. § 548.14 is not designed to excuse a party from exercising due diligence in preparing for trial. A judgment will not be vacated under the statute to enable a party to make a defense that ought to have been asserted in

the original action in the exercise of due diligence. See Wann v. Northwestern Trust Co., 120 Minn. 493, 498, 139 N.W.1061 (1913).

In this case, Tudor Oaks' limited partnership declaration expired in Ontario on August 19, 1990 and ABIO, Tudor Oak's general partner, had been involuntarily dissolved in Minnesota, thereby dissolving Tudor Oaks, in October of 1991. The trial court did not enter judgment in the original case until September 24, 1992. The expired registration status of the Tudor Oaks partnership was available to Cochrane through public record at any time during that first trial. Cochrane cannot now raise a defense that should have been raised during the first trial.

Plaintiff's cite extensively to Halloran v. Blue and White Liberty Cab Co., 253 Minn. 436, 92 N.W.2d 794 (1958), to support its position that the Court should deny summary judgment. The Halloran Court states that "[a] judgment may be set aside at any time for after-discovered fraud upon the court." In this case, however, the "fraud" claimed by Plaintiffs could have been discovered at anytime during the first lawsuit. The information was easily available through public record and therefore, the Plaintiff cannot now raise a defense that should have been raised in the prior lawsuit.

D. The Realignment Did Not Change The Result Of The Diversity Issue.

Plaintiffs allege in the Complaint that the purchase made by McLaughlin of all of the interests in Tudor Oaks was

concealed from the Federal Court. Furthermore, Plaintiffs argue that if the sale had not been concealed from the Court, the diversity of citizenship of the parties would not have been defeated and jurisdiction over this matter would have remained withe the Federal Court. Although Plaintiffs do not raise this issue in their Memorandum In Opposition to Defendant's Motion to Dismiss, the Defendant addressed the issue of the realignment of parties.

Defendant correctly asserts that even if the parties were not realigned, diversity still would not have existed because S. B. McLaughlin, a Canadian citizen, had the same citizenship as Tudor Oaks, which was a Canadian limited partnership. When the parties were realigned, there was not diversity because ABIO Holdings was a Minnesota corporation and KSCS Properties was a Minnesota corporation. Therefore, as a matter of law, the Federal Court could not have maintained jurisdiction over this matter regardless of whether realignment was properly granted.

"It is desirable that maters closed by a decree should be set at rest, and misrepresentations, to warrant the court in vacating a decree, should be of a tangible and substantial character." Wann, 120 Minn. At 498. In this case, the sale of interest in Tudor Oaks and ABIO, resulting in the realignment of the parties, is not substantial in character because the parties lacked diversity for Federal Court prior to the realignment. Therefore, this matter is not substantial in Character and should remain closed.

E. Whether The Nonexistence of Tudor Oaks and ABIO Constitutes Fraud is A Factual Issue.

Minnesota Statute § 548.14, is intended to provide relief from judgments obtained though fraud upon the court. The fraud must be of a substantial character and must be proved unequivocally. The Supreme Court has stated that fraud on the court must be an intentional course of material misrepresentation or nondisclosure, having the result of misleading the court and opposing counsel. Maranda v. Maranda, 449 N.W.2d 158, 165 (Minn. 1989).

The Court in Halloran v. Blue and White Liberty Cab Co. Inc., 253 Minn. 436, 443, 92 N.W.2d 794 (1958), states,

> "[W]here a party intentionally misleads or deceives the court as to the identity of a litigant and permits the court to wast its time on the trial of an action against a nonexisting party, such conduct constitutes a fraud upon the court."

However, the Court went on to note that a defense may be undertaken as a routine matter without knowing at the time that the defendant for which they appeared did not exist.

The same may be found in the present case. While the issue has been raised as to whether or not the court was misled by the conduct of the S.B. McLaughlin, Tudor Oaks, ABIO and their attorney in the original action, it should be made clear that the record does not establish as a matter of law, that the court was deceived or intentionally misled. Regardless of whether or not fraud was actually perpetrated

upon the Court, the issue still remains whether the judgment was actually obtained through fraud.

F. Even If The Expiration of the Partnerships Was Concealed From The Court In A Fraudulent Manner, The Judgment Itself Was Not Obtained Through Fraud.

Defendant argues that even if Plaintiffs' allegations are true and the fact that Tudor Oaks and ABIO's partnerships had expired was fraudulently kept from the Court, the alleged "fraud" would have no impact on the outcome of the litigation.

Plaintiffs are correct in asserting that Minnesota Statute § 322A.69 recognizes that the laws of the State under which a foreign limited partnership is organized govern its organization and internal affairs. Therefore, Ontario law will govern the organization and internal affairs of Tudor Oaks. Under Ontario law, the dissolution of a corporate general partner dissolves a limited partnership unless the business is continued by the remaining general partners. Limited Partnership Act, Ch. 241, § 20 and Ch. L. 16, § 21. In this case, Tudor Oaks was dissolved upon the dissolution of its sole general partner, ABIO.

Under the laws of Ontario,

> "No limited partnership in respect of which a new declaration or a declaration of change has not been filed as required by section 18 and no member thereof is capable of maintaining any action or other proceeding in any court in

> Ontario in respect of any contractor tort made or arising in connection with the business carried on by the limited partnership."

Limited Partnership Act, Revised Statutes of Ontario 1980, Chapter 241, Section 19(1). Also, the Business Information Statute Law Amendment Act or Section 20 or Chapter L. 16, Limited Partnership Act, Revised Statutes of Ontario 1990 state:

> "No limited partnership that has unpaid fees or penalties or in respect of which a declaration has not been filed as required by this Act and no member thereof is capable of maintaining a proceeding in a court in Ontario in respect of the business carried on by the limited partnership except with leave of the court."

In this case, Tudor Oaks did have unpaid fees and had not filed a declaration. Furthermore, Tudor Oaks did not request the Court to grant leave from these requirements. The Court may grant leave if the Court is satisfied that "the failure to pay the fees or penalties or file the declaration was inadvertent". Id. The Court never made a finding that either Tudor Oaks or ABIO inadvertently failed to pay the partnership fees.

The Plaintiffs in this case did not raise the defense that Tudor Oaks was no longer a limited partnership while the initial action was proceeding. Whether a motion to vacate a judgment is made within a reasonable time depends upon all

of the facts and circumstances involved. In determining whether a motion is timely, the Court may consider whether any prejudice will result to the other party if the motion is granted. Simons v. Schiek's, Inc., 275 Minn. 132, 138-139, 145 N.W. 2d 548 (1966). The Court finds that the Plaintiffs' motion to vacate the judgment is not timely. The defendant, Tudor Oaks, is unable to request a leave of the court as provided by Ontario law to allow the court to make a finding that the failure to pay the fees was inadvertent.

Also, had the issue been raised during the initial proceeding, Tudor Oaks could have solved the problem by paying a renewal fee along with an additional fee. This would have restored the limited partnership retroactively from the date that the partnership was dissolved. Ontario Limited Partnership Act § 3(4). ABIO could also have retroactively restored its corporate status through filing a single annual registration and paying a $25.00 fee under Minnesota Statute § 302A.821, subd. 6. This is no longer possible because of a 1993 amendment to that statute. Therefore, the Court finds that the prejudice which will result to the defendant, Tudor Oaks, outweighs the Plaintiffs' motion to vacate the judgment.

Furthermore, even if the defense was raised in a timely manner, Ontario Partnership Act, section 38, provides that,

> "After the dissolution of a partnership, the authority of each partner to bind the firm and other rights and obligations of the partners continue despite the dissolution so far as is

> necessary to wind up the affairs of the partnership and to complete transactions begun but unfinished at the time of the dissolution,..."

Therefore, even though Tudor Oaks did not have a right to maintain any action, the only remaining partner, S.B. McLaughlin had a right to continue the action commenced before the partnership dissolved.

JGL

STATE OF MINNESOTA

IN COURT OF APPEALS
C4-92-2081

HENNEPIN COUNTY — Crippen, Judge
District Court File No. 87-11035

S.B. McLaughlin & Company, Ltd., et al.,

Respondents,

Wood R. Foster, Jr.
Jordan M. Lewis
Siegel, Brill,
Greupner & Duffy
1300 Washington
Avenue South
Minneapolis, MN
55401

vs.

John Cochrane,

Appellant (C4-92-2081),

David F. Herr
Mary R. Vasaly
Maslon Edelman
Borman & Brand
3300 Norwest Center
90 South 7th Street
Minneapolis, MN
55402

KSCS Properties, Inc.

Appellant (C6-92-2082).

Laura Jean Hanson
Charles E. Spevacek
Meagher & Geer
4200 Multifoods
Tower
33 South 6th Street
Minneapolis, MN
55402

Filed: June 29, 1993
Office of Appellate Courts

Considered and decided by Crippen, Presiding Judge, Lansing, Judge, and Randall, Judge.

UNPUBLISHED OPINION

CRIPPEN, Judge

This appeal raises numerous issues about damage awards premised on claims that appellant John Cochrane breached his fiduciary duties and that there was a conspiracy in this breach between Cochrane and several investment partners. We reverse in part and affirm in part with material modifications.

FACTS

The claims here are pursued by Tudor Oaks Limited Partnership; ABIO Holdings, Inc. its general partner; and S.B. McLaughlin & Company, Limited, one of its limited partners. Tudor Oaks bought property in Eden Prairie, Minnesota, to develop a condominium project. The enterprise failed and

First Bank foreclosed on the development parcel. This litigation arises out of First Bank's decision to sell its sheriff's certificate for a sum far below its stated value. On June 12, 1986, First Bank had purchased the property for $5.6 million, and on December 17, 1986, it sold that property for $1.2 million.

Following foreclosure, the bank initiated a deficiency proceeding for $3.5 million against Tudor Oaks and its partners. Two of the three partners retained appellant John Cochrane to represent themselves and the limited partnership for a $20,000 fee. Respondent McLaughlin & Company proceeded with its defenses independently. In attempting to sell its sheriff's certificate, First Bank offered to release the limited partnership and its partners from he deficiency claims.

Cochrane arranged for several investors, including himself, to purchase the sheriff's certificate for $1.2 million. He and his clients agreed that he would retain a 20 percent interest in the property as a fee for arranging the purchase. Sixty percent of the property was purchased by appellant KSCS Properties, Inc. of which Cochrane was a one quarter shareholder. Cochrane and each of his three partners contributed $300,000 for the sale. The remaining 20 percent interest, which at one point was expected to be transferred to Tudor Oaks, was alternatively put in the names of two of KSCS's shareholders, Roland Stinski and Bill Keefer, Sr.

In 1987, McLaughlin & Company, Tudor Oaks and ABIO sued for damages, claiming Cochrane breached his fiduciary

duty by (1) taking a 20 percent interest in the property as a fee for finding purchasers; (2) purchasing an undisclosed 15 percent interest in the property through his investment in KSCS; and (3) failing to represent his clients by permitting KSCS shareholders Stinski and Keefer to take the 20 percent interest expected to go to Tudor Oaks. The plaintiffs also claimed that KSCS conspired with Cochrane in all these breaches.

After trial, the jury awarded Tudor Oaks $1.628 million from Cochrane and $3.52 million from KSCS. It awarded McLaughlin & Company $792,00 from Cochrane. Appellants contend Cochrane owed no fiduciary duty to McLaughlin & Company and that the jury verdict involves material inconsistencies.

DECISION

1. Calculation of the Verdict.

Respondent maintains that the verdict calculations are largely consistent with its arguments to the jury. Although appellants challenge the logic of various calculations, they do not dispute respondent's description of how the calculations were made. In sum, the material calculations are as follows.

a. Respondent first explains the calculation of $3.52 million (Tudor Oaks' recovery from KSCS) as 55 percent of the real value of the sheriff's certificate after reducing that value by $300,000 for the sum Cochrane invested. The 55 percent represented Cochrane's 15 percent purchased interest; the 20 percent interest taken as a fee to arrange the purchase;

and the 20 percent "carried interest," which was originally expected to go to Tudor Oaks. The figure $3.52 million is 55 percent of $6.4 million. Respondent states that the jury had evidence that the sheriff's certificate was worth $6.7 million and that they reduced that figure by $300,000 in calculating damages.

b. Respondent explains that the jury calculated the remaining awards, $1.628 million (Tudor Oaks' recovery from Cochrane) and $792,000 (McLaughlin & Company's recovery from Cochrane) by adjusting the $3.52 million assessed against KSCS. Respondent states that the jury excluded from the $3.52 million the 20 percent "carried interest" taken by Stinski and Keefer. Respondent observes that the jury shared damages for that interest to the conspiracy but not to Cochrane himself. The remainder, $2.4 million was divided into thirds representing the three major interests in Tudor Oaks. One third, or $792,000, was awarded to McLaughlin & Company, and two thirds was awarded to Tudor Oaks. The jury increased the award to Tudor Oaks by $20,000 to include recovery of the attorney fees paid Cochrane when he was first retained in the deficiency suit. The preceding calculations present problems, which are addressed later in this opinion.

2. Carried Interest

Appellant KSCS contends the damages charged to the conspiracy could not exceed the amount attributed to the

underlying tort. The record confirms that damages charged to KSCS were based solely on allegations that it conspired in connection with Cochrane's breach of fiduciary duty to his clients. There was no independent basis for a claim of liability by KSCS. See Harding v. Ohio Cas. Ins. Co., 230 Minn. 327, 337-39, 41 N.W.2d 818, 825 (1950). Thus, the liability of KSCS cannot exceed the liability we ultimately determine for Cochrane. Id. at 338, 42 N.W. 2d at 825 (conspiracy permits vicarious liability and joinder of joint tortfeasors); see also Harrell v. 20th Century Ins. Co., 934 F.2d203, 208 (9th Cir. 1991); Doctors' Co. v. Superior Court, 775 p.2d 508, 510-11 (Cal.1989); Mills v. Murray, 472 S.W.2d 6, 12-13 (Mo. App. 1971).

We recognize that reconciling the verdict tends to eliminate any award of damage for the carried interest. It is evident that the jury included damage for this item in the calculation of liability of the conspirators, but not in the liability of Cochrane. We recognize also that the jury found Cochrane breached his fiduciary duty to his clients in connection with the loss of the carried interest, even though it made no award against him on these grounds. By notice of review, respondent asks that the verdict against Cochrane be increased to equal the verdict against the conspirators. We are not at liberty to increase the award against Cochrane. There was ample evidence permitting the jury to attribute no harm to Cochrane from his role in dealing with the parties regarding the carried interest. Respondents have recognized

that the jury declined an award against Cochrane on that basis, and we are compelled to affirm that decision on the existing record.

3. Calculation of Cochrane's Liability

Respondent acknowledges the damage calculation began with use of a figure of $6.7 million, representing the value of the sheriff's certificate in December 1986. The jury's verdict, however, included a specific finding that the value of the certificate was $5.6 million, and that figure is abundantly confirmed by evidence of record. This court may reconcile the jury's answers based on the trial court record, as long as it does not interfere with the jury's fact-finding role. See Bogut v. Jannetta, 410 N.W.2d 451, 454 (Minn.App. 1987).

Using the correct valuation, the jury's calculation would proceed in this fashion. The jury would take $5.6 million, subtract $300,000 invested by Cochrane, and multiply that figure by 35 percent, which represents the 20 percent interest taken by Cochrane as a fee for arranging the purchase and his 15 percent purchased interest. Thirty-five percent of $5.3 million is $1.855 million. The jury decided to award two-thirds of this sum ($1,236,666) to Tudor Oaks and to increase that sum by the $20,000 attorney fee Tudor Oaks paid Cochrane. Thus the award to Tudor Oaks should total $1,256,666.

The jury was asked to state separately the damage awards against Cochrane and the conspiracy. Appellants contend that

there should be a single award of joint and several liability to Cochrane and to KSCS. Respondent conceded that point to the trial court, but contends the issue is not properly preserved for appeal. The issue is before us. Appellant clearly raised the issue in post-trial briefs, which challenged the amount of damages awarded and the consistency of the calculations of the verdict. Cochrane and KSCS have joint and several liability on the $1,256,666 verdict in favor of Tudor Oaks.

4. Separate Award to McLaughlin

Respondents proposed to the jury that there be a separate award of damages in favor of McLaughlin & Company. The jury apparently apportioned between Tudor Oaks and McLaughlin & Company the damages attributable to Cochrane's taking of the 20 percent interest as a fee and the 15 percent interest by purchase. The jury concluded that damages totaled $2.4 million, and of that amount, $790,000 should go to McLaughlin & Company. Consistent with the recalculation of the verdict previously stated in this opinion, the one third interest would be $618,333 (one third of 35 percent of $5.3 million).[2]

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[2]At Trial, respondent argued that the jury should award McLaughlin & Company damages resulting from its lost opportunity to purchase the property. Respondent asked the jury to award the value of the property, e.g., $5.6 million, minus the amount it would have cost McLaughlin & Company to purchase it, $1.2 million. We cannot explain why the jury measured separate damages for McLaughlin & Company as one third of the total

Appellants contend that the award of damages to McLaughlin & Company must be set aside, because Cochrane owed the company no fiduciary duty.[3] This position is consistent with existing Minnesota law stating that lawyers have a limited duty to persons other than their clients. See Marker v. Greenberg, 313 N.W.2d 4, 5, (Minn.1981); Schuler v. Meschke, 435 N.W.2d 156, 163 (Minn. App. 1989) pet. for rev. denied (Minn. Apr. 19, 1989). Even if we were to hold that an attorney for a partnership owes a fiduciary duty to each partner, that rule would be inappropriate in circumstances such as these where one partner was separately

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damages caused to Tudor Oaks. Because McLaughlin & Company has an interest in Tudor Oaks, any separate award to McLaughlin & Company is seemingly enhanced by the portion of Tudor Oak's award it would be entitled to receive. However, illogical, it is evident the jury used the one third formula in calculating the award. Because we set aside this award for other reasons, we need not further explore this calculation.

[3]The trial court permitted the jury to determine whether Cochrane owed a fiduciary duty to McLaughlin & Company, even though respondent admitted that no attorney-client relationship existed. Because the facts were undisputed , the trial court should have determined as a matter of law whether Cochrane owed a fiduciary duty, and we review that issue independently on the record. See Lind v. Slowinski, 450 N.W.2d 353, 356 (Minn. App. 1990) (The existence of a legal duty is a question of law) pet. for rev. denied (Minn. Feb. 21, 1990); see also A.J. Chromy Constr. Co. v. Commercial Mechanical Services, Inc., 260 N.W.2d 579, 582 (Minn.1977) (district court's legal conclusions are not binding on this court).

represented and deliberately acted independently of the lawyer serving the entity. Under these circumstances. Cochrane owed no fiduciary duty to McLaughlin & Company.

Because Cochrane did not owe a fiduciary duty to McLaughlin & Company, the damages awarded to it cannot be legally sustained. While logic might support an award to Tudor Oaks of $1,874,999, a combination of separate awards to Tudor Oaks and McLaughlin & Company, we are not at liberty to reapportion the damages, nor have we been asked to do so. Respondent submitted the case for separate awards and Tudor Oaks is entitled to the award as it was given and as now recalculated.

5. Other Issues.

a. Appellant Cochrane alleges that Tudor Oaks could not sue because an independent committee established by the general partner, ABIO Holdings, Inc., decided the suit was not in its best interests. See Minn. Stat. § 302A.243 (1988) (repealed in 1989; current version at Minn. Stat. § 302A.241 (1992)). Whether a suit is properly initiated is an issue among the three Tudor Oaks partners who controlled ABIO.[4]

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[4]The record indicates that the Tudor Oaks claim is now pursued singularly by S.B. McLaughlin. By 1989, he had purchased the interests of all the partners in Tudor Oaks. Appellants have not asserted and we have not explored issues surrounding McLaughlin's acquisition of benefits of suit by purchasing the interests of his partners. In fact, nothing in this record satisfactorily reflects the persons entitled to benefit from the

Cochrane, who was not a member of ABIO or Tudor Oaks, may not use the statute as a shield against liability.

b. Appellant contends that respondent failed to prove causation. The record provides adequate evidence to support the jury's finding that Cochrane's breach of fiduciary duty and his conspiracy with KSCS caused damage to Tudor Oaks.

c. Appellant Cochrane argues that the trial court improperly permitted an expert to testify about the rules of professional responsibility. Appellant contends that these rules provided the wrong standard of care for the jury in determining breach of fiduciary duty.

The ethics rules do not create a private cause of action. See Carlson v. Fredrikson & Byron, P.A., 475 N.W.2d 882, 889 (Minn. App. 1991) pet for rev. denied (Minn. Oct. 31, 1991). Use of these rules, however, is permitted where they will assist the jury in understanding the legal duty owed by an attorney, and where they are not presented as having the effect of a law. See e.g., Miami Int'l Realty Co. v. Paynter, 841 F.2d 348, 353 (10th Cir. 1988) (expert did not represent that deviations from ethics rules constituted negligence per se); Nagy v. Beckley, 578 N.E.2d 1134, 1137 (Ill. App. 1991) (it would be anomalous to hold that professional standards of ethics are not relevant considerations in tort action); Hizey v. Carpenter, 830 p.2d 646, 654 (Wash. 1992) (expert must testify generally about ethical requirements and may conclude

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ultimate judgment in favor of Tudor Oaks.

that the attorney's violations of the ethical rules constituted a deviation from the legal standard of care).

These proceedings involved reference to an unusual number of ethical standards. Our review of these references shows no instance in which the ethical standards were presented as constituting the legal duty of care. Additionally, the trial court properly instructed the jury that the violation of the rules did not establish a cause of action, but that the jury could consider them in determining whether Cochrane breached his fiduciary duties.

d. Appellant KSCS contends the evidence does not support the verdict because the jury should have offset the award to Tudor Oaks by its benefit in getting the $3.5 million deficiency release. The record shows, however, that had Tudor Oaks purchased the property, it would have been released from the deficiency, and it would have obtained property worth $5.6 million for a price of $1.2 million. This aspect of the verdict is supported by evidence of record.

e. Cochrane disputes various trial court instructions, including one stating that where an attorney and his client transfer business opportunities, the attorney must prove the fairness of the transaction. Appellant's motion for new trial does not address these instructions, and appellant has failed to preserve these issues for appeal. See Sauter v. Wasemiller, 389 N.W.2d 200, 201 (Minn.1986).

f. Appellants contend the trial court erred in excluding evidence of communications between McLaughlin

& Company and its attorneys regarding its attempts to purchase the property. Appellants sought to question the attorneys to determine whether McLaughlin & Company had the desire and the ability to purchase the sheriff's certificate. Appellants argue respondent S.B. McLaughlin waived the attorney-client privilege by testifying about directions he gave to his attorneys. See Swanson v. Domning, 251 Minn. 110, 118, 86 N.W.2d 716, 722 (1957) (where client voluntarily testifies about statements made to attorney, client waives the privilege on those things testified to and the adverse party may call the attorney as a witness to rebut or complete the conversation). Respondent incorrectly argues that the issue was not preserved for appeal.

Our review of the record shows S. B. McLaughlin testified that he instructed his attorneys to make an offer to the bank. He also produced evidence that he had funds available for purchase of the sheriff's certificate. McLaughlin & company's attorney, John Thiel, testified that he called the bank to inform it that McLaughlin was "proceeding * * * to meet the terms of the bank's letter," and that the bank then told him that Cochrane had already submitted an offer. McLaughlin's limited references to communications with his attorney did not constitute a complete waiver of the attorney-client privilege, and his attorney testified and was cross-examined about the topics McLaughlin had opened for discussion. The trial court did not err in suppressing evidence of additional communications between McLaughlin and his

attorneys.

g. Appellant KSCS argues that respondent failed to establish a claim for conspiracy because it failed to prove KSCS knowingly participated in the breach. The evidence shows that at least one other KSCS shareholder, Bertil Sandberg, knew about the 20 percent fee charged to find purchasers, and the record otherwise provides sufficient evidence to support the jury's finding that KSCS conspired with Cochrane to breach his fiduciary duty.

h. By notice of review, respondent requests this court to impose a constructive trust on the property. Courts have imposed constructive trusts where someone wrongfully obtains legal title to another's property by taking advantage of a fiduciary or confidential relationship. See e.g., Dietz v. Dietz, 244 Minn. 330, 334, 70 N.W.2d 281, 285 (1955). Courts also have imposed a constructive trust on property purchased with wrongfully obtained property. See e.g., Fingerhut Corp. v. Suburban Nat'l Bank, 460 N.W.2d 63, 67 (Minn. App. 1990). We have found no authority, however, for imposing a constructive trust in a situation like this one. Tudor Oaks lost the development property through foreclosure. The bank then offered to sell the property to anyone who could pay cash for it. Because the property did not belong to Tudor Oaks, we affirm the trial court's decision to deny a constructive trust.

In sum, we reverse the award of damages to McLaughlin & Company. We affirm the award to Tudor Oaks as modified

to $1,256,666, and reiterate that Cochrane and KSCS are jointly and severally liable for these damages.

Reversed in part and affirmed in part as modified.

/s/ Judge Crippen
June 22, 1993

STATE OF MINNESOTA	DISTRICT COURT
COUNTY OF HENNEPIN	FOURTH JUDICIAL DISTRICT

S. B. McLaughlin & Company, Ltd., Tudor Oaks Condominium Project, an Ontario Limited Partnership; ABIO Holdings (Minnesota) Inc., A Minnesota corporation, Plaintiffs,	TRANSCRIPT OF PROCEEDINGS VOLUME 2
vs.	File No. 87-11035
John Cochrane, an individual, and KSCS Properties, Inc., a Minnesota corporation, Defendants.	

The above-entitled matter came on for trial before the Honorable Gary Larson, a District Court judge, and a jury, commencing on the 2nd day of June, 1992, in the Hennepin County Government Center, City of Minneapolis, County of Hennepin and State of Minnesota.

APPEARANCES

Wood R. Foster, Jr., Esq., and Jordan M. Lewis, Esq., appeared as counsel for and on behalf of the plaintiffs.

Douglas Thompson and Stewart C. Loper, Esq., appeared as counsel for an on behalf of defendant John Cochrane.

James J. Schumacher, Esq., appeared as counsel for and on behalf of defendant KSCS Properties, Inc.

John A. Cochrane, defendant, appeared pro se.

* * * * *Page 136* * * * *

Stuart McLaughlin - Cross

A. That was a piece of not too complex restructuring and actually we were going to become a purchaser that was not otherwise available.

Q. Okay. Now, you couldn't put any money in ABIO or into Tudor Oaks to purchase a certificate because there were liens against them and that money would have been liened, isn't that true?

A. Well, when you have a sinking partnership, if you putmore money, fresh money it goes down the drain, you'recorrect.

Q. Now, --

A. Do you want me to do the next paragraph?

Q. Yes, please do.

A. "Five. I intend to carry out the purchase of the

Castle Ridge property and I and all partners will suffer substantial damages if the results turn out tobe otherwise. Six. It has been my efforts, in accordance with our contract which has brought about the opportunity to make the purchase from First St. Paul." And then there is several general paragraphs.

"This memo is also to call upon you to immediately, underlined, "advise the First National Bank of St. Paul that you will not cooperate with David Owen and that you are, in fact, cooperating with. . .

APPENDIX E

AGREEMENT
Page 117

AFFIDAVIT OF S. BRUCE MCLAUGHLIN
March 11, 1994
Page 140

RELATED CORRESPONDENCE
Page 142

AGREEMENT

THIS AGREEMENT made and entered into as of this 17th day of December, 1986 by and among K. S. C. S. PROPERTIES, INC., a Minnesota corporation (the "Purchaser"), TUDOR OAKS CONDOMINIUM PROJECT, an Ontario Limited Partnership ("Tudor Oaks"), ABIO HOLDINGS (MINNESOTA), INC., a Minnesota corporation ("ABIO"), DAVID S. OWEN ("Owen"), OWNIX DEVELOPMENTS LIMITED, an Ontario Corporation ("ODL"), J. D. CRASHLEY ("Crashley"), CENTRAL PRECISION LIMITED, an Ontario corporation ("CPL"), and THE FIRST NATIONAL BANK OF SAINT PAUL, a national banking association (the "Bank");

RECITALS:

1. At the request of Tudor Oaks and in accordance with the terms of that certain Construction Loan Agreement dated August 5, 1980 by and between the Bank and Tudor Oaks, the Bank made a construction loan to Tudor Oaks in the amount of $10,500,000.00 U.S. Tudor Oaks' obligation to repay the loan was evidenced by a certain Promissory Note dated August 5, 1980 made payable to the Bank's order by Tudor Oaks (the "Note"). Tudor Oaks obligations under the Note and Construction Loan Agreement were secured pursuant to the terms of a certain Statutory Mortgage,

Assignment of Leases and Rents and Security Agreement date August 5, 1980 which was executed by Tudor Oaks in favor of the Bank and recorded in the office of Hennepin County Recorder on August 6, 1980 as Document No. 4579607 (the "Mortgage"); and

2. On or about March 1, 1983 and December 28, 1984 the Bank and Tudor Oaks executed an Extension of Mortgage Agreement and an Agreement whereby the terms of the Note and Mortgage were extended and amended (hereinafter said Extension of Mortgage Agreement and Agreement will be collectively referred to as the "Amendments"); and

3. Repayment of the Note was severally guaranteed by Owen, S. B. McLaughlin & Co. Limited, an Ontario corporation ("SBML") and S. B. McLaughlin ("McLaughlin"), Crashley and CBL pursuant to the terms of certain separate Guaranties executed by them dated March 1, 1983 (the "Guaranties"). Tudor Oaks defaulted in the payment of the Note and under the terms and conditions of the Construction Loan Agreement, the Amendments and the Mortgage and upon said default the Bank demanded payment of all amounts outstanding on the Note and the Mortgage pursuant to certain demand letters dated January 23, 1986. Tudor Oaks failed to pay the amounts due to the Bank and following such default and failure to pay the bank commenced an action in Hennepin County District Court for the appointment of a receiver for the property then covered by the Mortgage which action is captioned The First National

Bank of Saint Paul vs. Tudor Oaks Condominium Project, et al., Court File No. MX 86-2999 (the "Receiver Action"); and

4. In addition, the Mortgage was duly and properly foreclosed by advertisement pursuant to Minnesota Statutes §580 and on June 12, 1986, the property then covered by the mortgage was sold by the Sheriff of Hennepin County at t mortgage foreclosure sale; and

5. Notice of such foreclosure sale was duly and properly served upon Tudor Oaks, ABIO, Owen, McLaughlin, SBML, Crashley and CPL prior to the foreclosure sale. Plaintiff was the highest bidder for the property offered for sale by the Sheriff and bid in at the foreclosure sale the total amount of $5,068,762.00 U.S. The Bank was awarded a Sheriff's Certificate of Sale dated June 12, 1986 (the "Sheriff's Certificate") which Sheriff's Certificate was recorded in the office of the Hennepin County Recorder on June 12, 1986 as Document No. 5118556 and covered certain property described therein (hereinafter said property will be collectively referred to as the "Project"); and

6. The Bank's foreclosure sale left an unpaid deficiency under the Note in the amount of $3,508,416,55 U.S. and on or about July 17, 1986, the Bank commenced an action in Hennepin County District Court which action is captioned The First National Bank of Saint Paul vs. Tudor Oaks Condominium Project, et al., Hennepin County District Court File No. 86-12931 (the"Deficiency Action"); and

7. The parties hereto desire to settle as to them the

Deficiency Action, to provide for the sale by the Bank and purchase by the purchaser of the Sheriff's Certificate and certain other rights which the Bank may have in the Project, and to provide for the substitution of the purchaser for the Bank as plaintiff in the Receiver Action, all as hereinafter set forth;

NOW, THEREFORE, the parties hereto hereby agree as follows:

1. Purchase and Sale.

1.1 Concurrently herewith Purchaser has paid to the Bank the sum of $1,200,000 U.S. in immediately available funds.

1.2 In consideration of the payment described in Section 1.1 above and the other agreements, releases, representations and covenants of Purchaser and the other parties hereto, the Bank has concurrently herewith executed and delivered or delivered to Purchaser the following:

1.2.1. Assignment of Sheriff's Certificate executed by the Bank whereby the Bank assigns to Purchaser its rights in the Sheriff's Certificate without recourse and without warranty of any type or kind.

1.2.2. Transfer of Special Declarant Rights

(the "Declarant Rights Transfer") whereby the Bank transfers to Purchaser all of its rights to exercise any special declarant rights under the Condominium Declaration relating to the Project.

1.2.3. Quit Claim Deed executed by the Bank in favor of the Purchaser.

1.2.4. Bill of Sale executed by the Bank in favor of the Purchaser.

1.2.5. Affidavit of Amount Due (the "Affidavit of Amount Due") executed by an officer of the Bank and detailing the sums expended by the Bank from June 13, 1986 to the date hereof.

1.2.6. Original ALTA Loan Policy - 1970 Rev. No. B 1419331 issued in favor of the Bank by Title Insurance Company of Minnesota (the "Title Policy").

1.2.7. Assignment of Title Policy executed by the Bank whereby the Bank assigns its rights in and to the Title Policy to

Purchaser without recourse and without warranty of any type or kind.

1.2.8. UCC-3 Assignment of Financing Statement.

1.3. ALL TRANSFERS AND ASSIGNMENTS BY THE BANK OF ITS RIGHT, TITLE AND INTEREST IN THE PROJECT OR ANY PART THEREOF ARE MADE BY THE BANK WITHOUT RECOURSE AND WITHOUT WARRANTY OF ANY TYPE OR KIND. ANY PROPERTY OR RIGHTS TO PROPERTY TRANSFERRED BY THE BANK TO PURCHASER ARE MADE "AS IS", WITHOUT ANY WARRANTY OF TITLE AND WITHOUT ANY EXPRESS OR IMPLIED WARRANTIES. THE BANK HEREBY DISCLAIMS ANY IMPLIED WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE WITH RESPECT TO ANY PROPERTY OR RIGHTS TO PROPERTY TRANSFERRED TO PURCHASER PURSUANT TO THIS AGREEMENT.

1.4. All fees and expenses necessary to record any of the documents delivered by the Bank to the Purchaser under Section 1.2 above including, but not

limited to, any recording and filing fees, state deed taxes, mortgage registration taxes, or other fees shall be the responsibility of and be paid by the Purchaser. Purchaser shall record the Assignment of Sheriff's Certificate, the Quitclaim Deed, Affidavit of Amount Due, and Declarant Rights Assignment within two days of the date hereof.

2. Substitution of Purchaser As Plaintiff in Receiver Action/Indemnity.

2.1 Purchaser hereby agrees to cooperate and do all things necessary to substitute the Purchaser for the Bank as the Plaintiff in the Receiver Action. Purchaser hereby further agrees and covenants to execute such documents, pleadings and instruments, as may be necessary in the judgment of the bank and its counsel, to effectuate such substitution.

2.2 Purchaser, Tudor Oaks, ABIO, Owen, ODL, Crashley, and CPL hereby jointly and severally agree to indemnify and hold the Bank harmless from any and all claims, causes of action, demands, liabilities, and costs (including, but not limited to attorneys' fees incurred by the Bank in defending or responding to any such claims, causes of action, demands or liabilities) which have been or may be asserted against the Bank by: (I) any party to the Receiver Action in the Receiver

Action from and after the date hereof; or (ii) any person or entity (including, but not limited to, any past, present or future resident or owner of any unit in the Castle Ridge condominiums) on account of the sale by the Bank of its interest in the Project to the Purchaser pursuant to the terms hereof; or (iii) any action or inaction of the Receiver in connection with the Project from and after the date hereof; or (iv) any action or inaction of the Purchaser or any other person subsequent to the Purchaser's purchase of the Sheriff's Certificate pursuant to the terms hereof.

3. Release. In consideration hereof, the parties hereto hereby agree to the following releases:

3.1 For purpose of Sections 3.2 through and including Section 3.7 hereof the term "Released Parties" shall mean, collectively and individually, the Bank, the Bank's parent, subsidiaries, and affiliates, all past, present, and future officers, directors, employees, solicitors, attorneys and agents of the Bank, the Bank's parent, subsidiaries and/or affiliates, and their respective heirs, personal representatives, successors and assigns.

3.2 Tudor Oaks hereby absolutely and unconditionally releases, waives, abandons and forever remises, discharges and releases the Released Parties (and

any of them) and their respective personal representatives, heirs, successors and assigns from any and all actions, causes of action, suits, debts, defenses, claims, counterclaims, and demands, whether known or unknown, which it ever had, now has or may hereafter have or which it could or may now or in the future assert against the Released parties (and any of them) in connection with any controversy arising out of or pertaining to the Project, any of the actions or inactions of the Released Parties (and any of them) with respect to the Project, and any of the documentation with respect to the Project and the documentation evidencing or securing any of the obligations or indebtedness of Tudor Oaks, ABIO, Owen, ODL, CPL, Crashley, McLaughlin, SBML and Participation Development Corporation (Minnesota), Inc., a Minnesota corporation ("PDC") (or any of them) to the Bank, including, without limitation, that certain Letter Loan Agreement dated February 15, 1980 by and between Tudor Oaks and the Bank and all documentation executed and delivered in connection therewith, the Construction Loan Agreement and all documentation delivered in connection therewith, that certain Amended Participation Agreement dated September 8, 1980 by and amount the Bank, SBML, ODL and CPL, the Amendments and all documents executed and delivered in connection therewith, that certain Letter Loan Agreement dated November 7, 1985 by and between Tudor Oaks and the

Bank and all documents executed and delivered in connection therewith, and all claims, causes of action, defenses, counterclaims, and demands which have been or might have been asserted against the Released Parties (and any of them) by Tudor Oaks in the Receiver Action and Deficiency Action.

3.3 ABIO hereby absolutely and unconditionally releases, waives, abandons and forever remises, discharges and releases the Released Parties (and any of them), from any and all actions, causes of action, suits, debts, defenses, claims, counterclaims, and demands, whether known or unknown, which it ever had, now has, or may hereafter have or which it could or may now or in the future assert against the Released Parties (and any of them) in connection with any controversy arising out of or pertaining to the Project, any of the actions or inactions of the Released Parties (and any of them) with respect tot he Project, and any of the documentation with respect to the Project and the documentation evidencing or securing any of the obligations or indebtedness of Tudor Oaks, ABIO, Owen, ODL, CPL, Crashley, McLaughlin, SBML and PDC (or any of them) to the Bank, including, without limitation, that certain Letter Loan Agreement dated February 15, 1980 by and between Tudor Oaks and the Bank and all documentation executed and delivered in connection

therewith, the Construction Loan Agreement and all documentation delivered in connection therewith, that certain Amended Participation Agreement dated September 8, 1980 by and among the Bank, SBML, ODL, and CPL, the Amendments and all documents executed and delivered in connection therewith, that certain Letter Loan Agreement dated November 7, 1985 by and between Tudor Oaks and the Bank and all documents executed and delivered in connection therewith, and all claims, causes of action, defenses, counterclaims, and demands which have been or might have been asserted against the Releases Parties (and any of them) by ABIO in the Receiver Action and Deficiency Action/

3.4 Owen hereby absolutely and unconditionally releases, waives, abandons and forever remises, discharges and releases the Released Parties (and any of them) from any and all actions, causes of action, suits, debts, defenses, claims, counterclaims, and demands, whether known or unknown, which he ever had, now has, or may hereafter have or which he could or may now or in the future assert against the Released Parties (and any of them) in connection with any controversy arising out of or pertaining to the Project, any of the actions of the Release Parties (and any of them) with respect to the Project, and any of the documentation with respect to the Project and the documentation evidencing

or securing any of the obligations or indebtedness of Tudor Oaks, ABIO, Owen, ODL, CPL, Crashley, McLaughlin, SBML, PDC (or any of them) to the Bank, including, without limitation, that certain Letter Loan Agreement dated February 15, 1980 by and between Tudor Oaks and the Bank and all documentation executed and delivered in connection therewith, the Construction Loan Agreement and all documentation delivered in connection therewith, that certain Amended Participation Agreement dated September 8, 1980 by and among the Bank, SBML, ODL and CPL, the Amendments and all documents executed and delivered in connection therewith, that certain Letter Loan Agreement dated November 7, 1985 by and between Tudor Oaks and the Bank and all documents executed and delivered in connection therewith, that certain Letter Loan Agreement dated November 7, 1985 by and between Tudor Oaks and the Bank and all documents executed and delivered in connection therewith, and all claims, causes of action, defenses, counterclaims, and demands which have been or might have been asserted against the Released Parties (and any of them) by Owen in the Receiver Action and Deficiency Action.

3.5 ODL hereby absolutely and unconditionally releases, waives, abandons and forever remises, discharges and releases the Released Parties (and

any of them) from any and all actions, causes of action, suits, debts, defenses, claims, counterclaims, and demands, whether known or unknown, which it ever had, now has, or may hereafter have or which it could or may now or in the future assert against the Released Parties (and any of them) in connection with any controversy arising out of or pertaining to the project, any of the actions or inactions of the Released Parties (and any of them) with respect to the Project, and any of the documentation with respect to the Project and the documentation evidencing or securing any of the obligations or indebtedness of Tudor Oaks, ABIO, Owen, ODL, CPL, Crashley, McLaughlin, SBML and PDC (or any of them) to the Bank, including, without limitation, that certain Letter loan Agreement dated February 15, 1980 by and between Tudor Oaks and the Bank and all documentation executed and delivered in connection therewith, the Construction Loan Agreement dated February 15, 1980 by and between Tudor Oaks and the Bank and all documentation executed and delivered in connection therewith, the Construction Loan Agreement and all documentation delivered in connection therewith, that certain Amended Participation Agreement dated September 8, 1980 by and among the Bank, SBML, ODL, and CPL, the Amendments and all documents executed and delivered in connection therewith, that certain Letter Loan Agreement dated November 7, 1985 by and between

Tudor Oaks and the Bank and all documents executed and delivered in connection therewith, and all claims, causes of action, defenses, counterclaims, and demands which have been or might have been asserted against the Released Parties (and any of them) by ODL in the Receiver Action and Deficiency Action.

3.6 Crashley hereby absolutely and unconditionally releases, waives, abandons and forever remises discharges and releases the Released Parties (and any of them) from any and all actions, causes of action, suits, debts, defenses, claims, counterclaims, and demands, whether known or unknown, which he ever had, now has, or may hereafter have or which he could or may now or in the future assert against the Released Parties (and any of them) in connection with any controversy arising out of or pertaining to the Project, any of the actions or inactions of the Released Parties (and any of them) with respect to the Project, and any of the documentation with respect to the Project, and nay of the documentation evidencing or securing any of the obligations or indebtedness of Tudor Oaks, ABIO, Owen, ODL, CPL, Crashley, McLaughlin, SBML, PDC (or any of them) to the Bank, including, without limitation that certain Letter Loan Agreement dated February 15, 1980 by and between Tudor Oaks and the Bank and all documentation executed and delivered in connection

therewith, the Construction Loan Agreement and all documentation delivered in connection therewith, that certain Amended Participation Agreement dated September 8, 1980 by and among the Bank, SBML, ODL and CPL, the Amendments and all documents executed and delivered in connection therewith, that certain Letter Loan Agreement dated November 7, 1985 by and between Tudor Oaks and the Bank and all documents executed and delivered in connection therewith, and all claims, causes of action, defenses, counterclaims, and demands which have been or might have been asserted against the Released Parties (and any of them) by Crashley in the Receiver Action and Deficiency Action.

3.7 CPL hereby absolutely and unconditionally releases, waives, abandons and forever remises, discharges and releases the Released Parties (and any of them) from any and all actions, causes of action, suits, debts, defenses, claims, counterclaims, and demands, whether known or unknown, which it ever had, now has, or may hereafter have or which it could or may now or in the future assert against the Released Parties (and any of them) in connection with any controversy arising out of or pertaining to the Project, any of the actions or inactions of the Released Parties (and any of them) with respect to the Project, and any of the documentation with respect to the Project and the

documentation evidencing or securing any of the obligations or indebtedness of Tudor Oaks, ABIO, Owen, ODL, CPL, Crashley, McLaughlin, SBML, and PDC (or any of them) to the Bank, including, without limitation, that certain letter Loan Agreement dated February 15, 1980 by and between Tudor Oaks and the Bank and all documentation executed and delivered in connection therewith, the Construction Loan Agreement and all documentation delivered in connection therewith, that certain Amended Participation Agreement dated September 8, 1980 by and among the Bank SBML, ODL and CPL, the Amendments and all documents executed and delivered in connection therewith, that certain Letter loan Agreement dated November 7, 1985 by and between Tudor Oaks and CPL and all documents executed and delivered in connection therewith, and all claims, causes of action, defenses, counterclaims, and demands which have been or might have been asserted against the Released Parties (and any of them) by CPL in the Receiver Action and Deficiency Action.

3.8 The Bank hereby absolutely and unconditionally releases and forever discharges Tudor Oaks, ABIO, Crashley, CPL, Owen, Ownix, their respective personal representatives, successors and assigns, from any and all actions, causes of action , suits and debts arising out of the claims made by the Bank in

the Deficiency Action. The Bank specifically reserves and retains any and all claims against Tudor Oaks, ABIO, Owen, Crashley, and CPL in connection with the following:

3.8.1. The Declarant Rights Transfer

3.8.2. That certain judgment entered in favor of the Bank against Tudor Oaks, ABIO, Owen, CPL and Crashley in the action venued in the Ramsey County Distrcit Court, captioned:

The First National Bank of Saint Paul v. Tudor Oaks Condominium Project, et al. Court File No. 477239

3.8.3. Any and all claims arising out of this Agreement.

In addition, the Bank specifically reserves and retains any all claims which it may now or in the future have against SBML, McLaughlin and PDC including, without limitation, all claims asserted by the bank against said persons (or any of them) in the Receiver Action or the Deficiency Action.

4. Dismissal of Deficiency Action. The Bank, Tudor Oaks, ABIO, Owen, Crashley and CPL hereby agree to dismiss with prejudice their respective claims and defenses in the Deficiency Action and hereby instruct their respective counsel to execute and file on their behalf a Stipulation of Dismissal With Prejudice and obtain an Order dismissing the Deficiency Action as to them with prejudice. The Deficiency Action shall not be dismissed as to SBML or McLaughlin.

5. Residential Health Options Action. Purchaser, Tudor Oaks, ABIO, Owen, Ownix, Crashley, and CPL acknowledge that they have been informed of the commencement of a certain action, by Residential Health Options, Inc. By and against ABIO, the Bank and James C. Melville in an action venued in Hennepin County District, captioned:

Residential Health Options, Inc.

vs.

ABIO Holdings (Minnesota), Inc
First Bank St. Paul, and
James C. Melville, individually

6. Representations and Warranties. To induce the bank to enter into this Agreement, the parties to this

Agreement other than the Bank represent and warrant to the Bank that:

6.1 They have been represented and advised by counsel in connection with the execution of this Agreement and the delivery of the documents contemplated hereby.

6.2 They and their counsel have independently examined and inspected the Project, the current status of title to the Project, all of the pleadings in the Receiver Action, the Deficiency Action, and the Residential Health Options Action, and such other documents and instruments as they have deemed necessary and appropriate to evaluate their respective entry into this Agreement and the purchase by the Purchaser of certain rights in the Project as contemplated by this Agreement and have relied upon no representations or warranties of the Bank or any of its past or present directors, officers, employees, agents, and attorneys.

6.3 Purchaser is a duly organized and validly existing Minnesota corporation with Wilbur C. Keefer, Roland A. Stinski, Bertil E. Sandberg, John A. Cochrane, and James R. Bresnahan as its sole shareholders and is in good standing and is qualified to do

business under the laws of the State of Minnesota.

6.4 Tudor Oaks is a duly organized and validly existing Ontario limited partnership and is in good standing under laws of the State of Minnesota.

6.5 ABIO is duly organized and validly existing Minnesota corporation and is in good standing and is qualified to do business under the laws of the State of Minnesota.

6.6 CPL and ODL are duly organized and validly existing Ontario corporations and are in good standing and are qualified to do business under the laws of the State of Minnesota.

6.7 Owen and Crashley are residents of Toronto, Ontario, Canada.

6.8 Each of them are duly authorized and empowered to execute, deliver and perform this Agreement and any other document or instrument to be executed by them or any of them pursuant hereto and all partnership and corporate action on their part (including any stockholder or partner consent or approval) requisite for the due execution, delivery and performance of this Agreement, and any other document or instrument to be

executed by them (or any of them) pursuant hereto has been duly and effectively taken.

6.9 This Agreement constitutes a legal, valid and binding obligation upon said parities, enforceable in accordance with its terms.

7. Recitals. The Parties hereto hereby agree that the Recitals set forth at the beginning of this Agreement are true and correct in all respects.

8. Governing Law/Venue. This Agreement and the rights and obligations of the parties hereunder shall be construed and governed by the laws of the State of Minnesota, U.S.A. All parties hereby consent to the personal jurisdiction of the state and federal courts located in the State of Minnesota in connection with any controversy related to this Agreement, waive any argument that venue in such forums is not convenient and agree that nay litigation instigated by them (or any of them) against the Bank in connection with this Agreement or any of the documents delivered hereunder shall be venued in either the District Courts of Ramsey County, Minnesota or the United States District Court for the District of Minnesota, Third Division.

9. Service of Process. Purchaser, Tudor Oaks, ABIO, Crashley, CPL, ODL and Owen hereby irrevocably

appoint John A. Cochrane and Ronald Alley as their respective agents for service of process and hereby consent to the personal and subject matter jurisdiction of the Courts of the State of Minnesota dn Federal Courts located within the State of Minnesota in connection with any controversy or proceeding arising under this Agreement.

10. Benefit/Burden. This Agreement shall be binding upon and inure to the benefit of the parties hereto and their respective personal representatives, successors and assigns.

11. Merger. This Agreement supercedes any prior agreements between the parties hereto concerning the subjects hereof.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed the date and year first above written.

PURCHASER: K.S.C.S. PROPERTIES, INC.
a Minnesota corporation
By /s/ Wilbur Taylor
Its Pres.

TUDOR OAKS: TUDOR OAKS CONDOMINIUM PROJECT
an Ontario Limited Partnership
By/s/ David Owen
President of ABIO Holdings

(Minnesota), Inc. Its
general partner

ABIO: ABIO HOLDINGS (MINNESOTA), INC.
BY /s/ David Owen
Its President

CRASHLEY: /s/ J. D. Crashley
J. D. CRASHLEY

CPL: CENTRAL PRECISION LIMITED, an Ontario Corporation
By /s/J. D. Crashley
Its Chairman

ODL: OWNIX DEVELOPMENTS LIMITED
BY /s/ David Owen
Its President

OWEN: /s/ David Owen
DAVID S. OWEN

BANK: THE FIRST NATIONAL BANK OF SAINT PAUL
By /s/ James Melville
Its Assistant Vice President

STATE OF MINNESOTA	DISTRICT COURT
COUNTY OF HENNEPIN	FOURTH JUDICIAL DISTRICT

John A. Cochrane,

Plaintiff,

Case No. 93-16553

v.

AFFIDAVIT OF S. BRUCE MCLAUGHLIN

Tudor Oaks Condominium Project, an Ontario Limited Partnership, Nul Tiel,

Defendant,

STATE OF MINNESOTA)
)ss.
COUNTY OF HENNEPIN)

S. BRUCE MCLAUGHLIN, being first duly sworn, on oath states.

1. That he is the president of S.B. McLaughlin & Co., Inc. A limited partner of the Tudor Oaks Condominium Project limited partnership.

2. That he is the liquidating trustee of the Tudor Oaks Condominium Project limited partnership.

3. That neither he nor his company ever received a notice of expiration concerning the limited partnership status in Ontario.

4. That neither he nor his company ever received notice of expiration from the Minnesota Secretary of States Office concerning the filing requirements of the Minnesota corporation that comprised the general partner of the Tudor Oaks Condominium Project limited partnership.

5. That, if indeed notice was sent, it must have been sent to one of the other limited partnership owners that had, heretofore, received notice on behalf of the partnership.

6. That neither these entities, nor the principals behind these entities ever passed notice onto S.B. McLaughlin & Co. or to S. Bruce McLaughlin at any time.

Further this Affiant sayeth not.

Dated: March 11, 1994

/s/ S. Bruce McLaughlin
S. Bruce McLaughlin

Subscribed and sworn to before me
this 11th day of March, 1994.
/s/C. Morgan
Notary Public

COCHRANE AND BRESNAHAN PA ST
24 EAST 4 ST
ST PAUL MN 55101

THIS IS A CONFIRMATION COPY OF THE FOLLOWING MESSAGE:

6122981950 TDBN ST PAUL MN 89 11-14 1015A EST
PMS DAVID OWEN, 4165984450
CARE LAWRENCE B. HEATH, Q.C.
214 KING ST. WEST SUITE 500 M5H1K4
TORONTO ON CAN
DEAR SIRS,
CONFIRMING OUR TELEPHONE AGREEMENT OF NOVEMBER 13, 1986 WE HAVE ARRANGED FOR 1.5 MILLION DOLLAR FINANCING TO PURCHASE THE SHERIFF'S CERTIFICATE FROM THE FIRST NTONAL BANK OF ST. PAUL ON THE TUDOR OAKS PROJECT.

UPON ACQUISITION OF THE CERTIFICATE THE FIRM OF COCHRANE AND BRESNAHAN, P.A. SHALL HAVE A 20 PERCENT INTEREST THEREON. THE FINANCING ENTITY A 60 PERCENT INTEREST THEREON AND OWENS/CRASHLEY INTERESTS SHALL HAVE A 20 PERCENT INTEREST THEREON.

YOU AUTHORIZED ME TO PROCEED ON THAT BASIS AND WE HAVE GONE FORWARD ON RELIANCE OF THAT AUTHORIZATION.

JOHN A COCHRANE

10:15 EST

MGMCOMP

November 11, 1986

"BY COURIER"

Mr. John A. Cochrane,
Attorneys at Law,
Cochrane and Bresnahan,
24 East Fourth Street,
Saint Paul, Minnesota 55101,
U.S.A.

Dear Mr. Cochrane:

Further to our telephone conversation of to-day we hereby authorize you to try and find an investor to invest the necessary funds to payout the First National Bank of Saint Paul on the Tudor Oaks Condominium project. If you have such an investor we are prepared to give you 20% of the lift and fully understand that you are not self dealing in such an arrangement. We also understand that the investor may require a substantial part of the lift also.

We trust that the aforesaid is satisfactory for your purposes.

Yours sincerely,
/s/Larry
Lawrence B. Heath, Q.C.

November 7, 1986

VIA MESSENGER

Mr. John A. Cochrane
Mr. Ronald D. Alley
Attorneys at Law
Cochrane and Bresnahan
24 East Fourth Street
Saint Paul, Minnesota 55101

Mr John Thiel
Mr. William L. Killion
Attorney at Law
Gray, Plant, Mooty, Mooty & Bennett
3400 City Center
33 South Sixth Street
Minneapolis, Minnesota 55402

Re: The First National Bank of Saint Paul (the "Bank") vs. Tudor Oaks Condominium Project, et al. Hennepin County District Court File No. 86-12931

Gentlemen:

For various business reasons the Bank has decided to attempt to sell the Sheriff's Certificate awarded to it at the foreclosure sale held on June 12, 1986 (the "Sheriff's Certificate") covering the remaining unsold units in the Castle Ridge Condominium Project (the "Project") at a substantial

discount provided such sale can be accomplished on or prior to December 17, 1986. In light of this decision it was thought that it might be possible to settle all or a portion of the above-referenced litigation upon the terms set forth below and, accordingly, we are authorized to make to your clients the following settlement proposal:

1. The Bank will transfer and assign the Sheriff's Certificate to any of the named defendants or a separate entity comprised of some or all of such defendants in return for $1,500,000.00 U.S. and the delivery of a written release from the defendants involved in the purchase of the Sheriff's Certificates. The Bank will not finance all or any part of the $1,500,000 payment and the assignment of the Sheriff's Certificates will be without recourse and without warranty of any type or kind on the part of the Bank.
2. In consideration of the payment of the $1,500,000 U. S. And the delivery of releases, the Bank will also dismiss with prejudice the above-referenced lawsuit against all defendants involved in the purchase of the Sheriff's Certificate providing the Bank with signed releases. The Bank will retain all of its claims against any defendants not involved in the purchase of the Sheriff's Certificate. The Bank will also retain all of its claims against any

defendants involved in the purchase who do not provide releases.

3. The purchaser of the Sheriff's Certificate must be substituted of record for the Bank as the plaintiff in the receivership action previously commenced by the Bank with respect to the Project which action is captioned The First National Bank of Saint Paul, Plaintiff, vs. Tudor Oak's Condominium Project, et al., Defendants, Court File No MX 86-2999 (the "Receiver Action"). In connection with such substitution, the Bank shall receive a written accounting from the Receiver for all sums expended to the date of the substitution.

4. The transaction must close and be fully completed on or before December 17, 1986. The closing shall be held in the offices of Briggs and Morgan, P. A.

5. All documentation evidencing or relating to the transfer of the Sheriff's Certificate, the releases, and the replacement of the Bank as plaintiff in the Receiver Action or otherwise involving the settlement shall be in form and substance acceptable to the Bank and this office.

6. This proposal is made for settlement purposes only and may not be introduced in evidence in any action nor be used for any purpose.

The Bank will be actively seeking other purchasers of its Sheriff's Certificate upon such terms as the Bank deems

appropriate, which terms may or may not be the same as set forth above, and reserves the right to sell the Sheriff's Certificate to the first acceptable purchaser that can close the transaction. Accordingly, the above proposal is not intended as an offer nor shall the Bank have any obligation to transfer the Sheriff's Certificate or to settle the above-referenced lawsuit with any of the defendants unless and until the transaction closes.

Because we have been contacted by and have had correspondence from some or all of the defendants' Canadian counsel and in light of the relatively short period of time during which the Bank is willing to sell the Sheriff's Certificate, we have taken the liberty of sending copies of this letter to such counsel for their information.

Please contact me as soon as possible if your clients are interested in pursuing this proposal.

Sincerely,
/s/ Charles R. Haynor
Charles R. Haynor
Richard G. Mark

RGM:dt
cc: James C. Melville
Charles R. Haynor, Esq.
Gordon Marantz, Esq.
Lorne Slatman, Esq.
Larry Heath, Esq.
William McClintock, Esq.
3/1

August 27, 1986

Lawrence B. Heath, Q.C.
214 King Street West
Suite 500
Toronto, Ontario M5H 1K4

Re: Tudor Oaks

Dear Mr. Heath:

It was indeed a pleasure meeting with you and briefly going over the Tudor Oaks litigation now pending in District Court, Hennepin County, Minnesota.

As I discussed with you, upon receipt of the executed Fee Agreement, enclosed with this letter, and the receipt by this firm of the $25,000 retainer, this firm will interpose Answers for:

1. David Owen and Ownix Development Limited
2. J. D. Crashley and Central Precision Limited
3. ABIO Holdings, Inc.
4. Tudor Oaks Condominium Project

and will undertake the defense of the matter for these Defendants. As Mr. Alley and I explained to you, it is a most difficult defense and your clients do have a great deal of exposure. We feel that there are some legitimate defenses

that may be interposed. Upon further research and investigation, if this firm is retained, we will keep you advised as to possible defenses.

We have been advised that the Grey, Plant, Mooty firm of Minneapolis will act for Mr. S. B. McLaughlin and his company.

As you are aware, time is of the essence in this matter as Answer is due by September 5, 1986.

Very truly yours,
/s/John A. Cochrane
John A. Cochrane

JAC:dp
Enclosure

Supreme Court, U.S.
FILED
JAN 12 1998
CLERK

(2)

No. 97-973

In The

Supreme Court of the United States

October Term, 1997

JOHN A. COCHRANE,

Petitioner,

vs.

TUDOR OAKS LIMITED PARTNERSHIP,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Eighth Circuit

RESPONDENT'S BRIEF IN OPPOSITION

WILLIAM J. FISHER
Counsel of Record
GRAY, PLANT, MOOTY,
MOOTY & BENNETT, P.A.
Attorneys for Respondent
Tudor Oaks Limited Partnership
by its Liquidating Trustee,
S.B. McLaughlin & Co.
3400 Multifoods Tower
33 South Sixth Street
Minneapolis, Minnesota 55402
(612) 343-2800

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STATEMENT OF THE CASE

This is a petition from an order of the Eighth Circuit Court of Appeals affirming a summary judgment order which found that a debt of the Petitioner to the Respondent was non-dischargeable in his bankruptcy. The debt arises from a State Court Judgment.

The following facts are based upon the findings of the jury in the State Court action between the two parties ("State Court Action") and the facts as stated by the Minnesota Court of Appeals in the appeal of that decision. The Bankruptcy Court's decision and Eighth Circuit Court of Appeal's decision also concisely summarizes the facts. Much of the Petitioner's Statement of the Case are "facts" which were not found by any Court and, actually, were rejected.

Tudor Oaks Limited Partnership ("Tudor Oaks" or "Respondent") retained the Petitioner to represent it for a $20,000 fee in a lawsuit commenced against the Respondent by First Bank Minnesota, N.A. involving a foreclosure on certain real estate and any deficiency amount arising after the foreclosure sale. (*See* Court of Appeals decision, a copy of which is included in Petitioner's Appendix at Apdx. 101.) The Petitioner then arranged for several investors, including himself, to purchase the Sheriff's Certificate at the foreclosure sale on that same real estate for $1.2 million. (Court of Appeals decision, Petitioner's Appendix at Apdx. 101.) The Respondent and the Petitioner agreed that the Petitioner would retain a twenty percent (20%) interest in the property as a fee for arranging the purchase. (Court of Appeals decision, Petitioner's Appendix at Apdx. 101.) Sixty percent (60%) of the property was purchased by KSCS Properties, Inc., of which Petitioner was a one-quarter (1/4) shareholder. (Court of Appeals decision, Petitioner's Appendix at Apdx. 101.) The Petitioner and his three partners

contributed $300,000 for the sale. (Court of Appeals decision, Petitioner's Appendix at Apdx. 101.) The remaining twenty percent (20%) was expected to be transferred to the Respondent. (Court of Appeals decision, Petitioner's Appendix at Apdx. 101.) Instead, the twenty percent (20%) interest was put in the name of two of the KSCS shareholders, Roland Stinski and Bill Keifer, Sr. (Court of Appeals decision, Petitioner's Appendix at Apdx. 101.)

The Respondent then sued the Petitioner for breach of fiduciary duty for: (1) taking the twenty percent (20%) interest in the property as a fee for finding purchasers; (2) purchasing an undisclosed fifteen percent (15%) interest in the property through the Petitioner's investment in KSCS; and (3) failing to represent the Respondent by permitting KSCS shareholders Stinski and Keifer to take the twenty percent (20%) interest expected to go to the Respondent. (Court of Appeals decision, Petitioner's Appendix at Apdx. 102.)

The Respondent prevailed at the trial in this matter. As a result of these breaches, judgment was entered in the amount of $1,628,000 (*See* Court of Appeals decision, Petitioner's Appendix at Apdx. 102.) The special verdict form shows the breaches of fiduciary duty. (A copy of the Special Verdict Form is included in Respondent's Appendix at 1a.)

The Petitioner appealed this decision. The Minnesota Court of Appeals affirmed the breach of fiduciary duty portion of the findings. The only change regarding the Respondent was that the damages were reduced from $1,628,000 to $1,256,666. The Respondent then sought to have the Order amended to include prejudgment interest and it was amended to include prejudgment interest of $465,339.52 as of April 11, 1994.

On December 22, 1992, the Petitioner filed for relief under Chapter 11 of Title 11 (bankruptcy) of the U.S. Code, and this

case was converted to Chapter 7 on February 15, 1994. This adversary proceeding, seeking an order finding that the debt of the Petitioner to the Respondent was non-dischargeable, was filed in a timely manner on May 20, 1994. The Petitioner answered the Complaint challenging the findings in the previous action.

The Petitioner also brought a lawsuit to vacate the judgment in State District Court in Minnesota. That State District Court lawsuit was dismissed. (A copy of the decision by the State District Court is at Apdx. 84 of the Petitioner's Appendix.) The Petitioner sought vacation of the judgment largely on the basis that it was obtained by fraud for failure to disclose the dissolution of the Respondent partnership. On that issue, Minnesota State District Judge Gary Larson found that the issue was irrelevant since,

> . . . even though Tudor Oaks did not have a right to maintain any action, the only remaining partner, S. B. McLaughlin had a right to continue the action commenced before the partnership dissolved.

(Petitioner's Appendix, at Apdx. 98.) It found that, as a matter of law, the fraud defense failed. The Minnesota Court of Appeals affirmed this decision. A copy of the Minnesota Court of Appeals opinion is at Apdx. 60 of Petitioner's Appendix. It is also published as *Cochrane v. Tudor Oaks Condominium Project*, 529 N.W. 2d 429 (Minn. App. 1995), *review denied*, (1995).

The Respondent moved for summary judgment in the Bankruptcy Court adversary proceeding on the basis of collateral estoppel. The Bankruptcy Court found that in this case the breach of fiduciary findings in the State Court could be applied to this action under the theory of collateral estoppel and that as to the standing issue (either under the theory of collateral estoppel or

as a matter of law) the action could be maintained by S.B. McLaughlin & Co., as liquidating trustee of Tudor Oaks Limited Partnership. The District Court affirmed the Bankruptcy Court order and the Eighth Circuit Court of Appeals affirmed the District Court. The Eighth Circuit found that the Respondent had standing as a matter of law, collateral estoppel applied, and the Petitioner committed a defalcation while acting in a fiduciary capacity. As a result, the debt was held non-dischargeable.

SUMMARY OF THE ARGUMENT

The Petitioner has presented four questions. The first question is whether a breach of fiduciary duty resulting in no damages can be a defalcation under 11 U.S.C. § 523(a)(4). There was a defalcation in this case and there were damages. The second and fourth questions addressed whether the Respondent has standing and whether collateral estoppel on the issue of standing applies. It is clear that the Respondent has standing as the remaining partner of a dissolved partnership. It is also clear that collateral estoppel was never applied by the Eighth Circuit Court of Appeals on this issue — it decided standing as a matter of law. Finally, the third question asked whether full, faith, and credit can be given to the state court proceeding when there are allegations the judgment was obtained by fraud. The Eighth Circuit Court of Appeals properly held that collateral estoppel did apply and the fraud argument failed as a matter of law. The standing, collateral estoppel, and defalcation issues will now be addressed.

REASONS FOR DENYING THE WRIT

I.

THE RESPONDENT HAS STANDING TO BRING THIS ACTION.

The Petitioner argues that the Respondent had no standing to bring this action. Assuming the Respondent is a dissolved partnership, it is clear that under Ontario law (the governing law) and the partnership agreement, the remaining partners of a dissolved partnership have the right to wind up the affairs of the partnership. Ontario Partnership Act Section 38 states,

> After the dissolution of a partnership, the authority of each partner to bind the firm and other rights and obligations of the partners continue despite the dissolution so far as is necessary to wind up the affairs of the partnership and to complete transactions begun but unfinished at the time of the dissolution, but not otherwise . . .

This was the finding of the State District Court and the Minnesota Court of Appeals. Accordingly, the only remaining partner, S.B. McLaughlin & Co. has a right to proceed in the Bankruptcy Court.

The Bankruptcy Court stated in footnote 17 of its Order at Apdx. 38-39 in the Petitioner's Appendix,

> Regardless of whether the named party-plaintiff is a valid, subsisting legal entity with capacity to sue or to be sued, its one remaining partner has the right under Ontario law to wind up its affairs and to continue litigation under its name to do so.

The Eighth Circuit agreed that the standing was a clear issue under Ontario law. It cited section 38 of the Ontario Partnership Act and held that ". . . McLaughlin has standing to litigate this bankruptcy matter in the name of Tudor Oaks." (Petitioner's Appendix at Apdx. 12.)

The Petitioner states in the fourth question presented that the standing ruling was made on the basis of collateral estoppel. In fact, the Eighth Circuit Court of Appeals specifically declined to apply collateral estoppel. (*See* Petitioner's Appendix at Apdx. 10.) Instead, it made this determination as a matter of Ontario law.

The assets, including a claim, do not disappear when a partnership is dissolved. The remaining partner or partners take control. It is that simple. The Petitioner never disputes this point; instead, he argues in pages 18-22 of his brief that the Respondent is a dissolved partnership. This issue is irrelevant because as the Bankruptcy Court and Eighth Circuit Court of Appeals correctly pointed out, the remaining partner, S.B. McLaughlin, may wind up the affairs of the dissolved partnership. The Respondent has standing as a matter of law.[1]

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1. The decision of *Appletree Square I Limited Partnership & Business Consultants, Inc. v. O'Connor & Hannon*, 559 N.W.2d 711 (Minn. App. 1997), *review granted*, (1997), cited by the Petitioner, has nothing to do with this case. That case involved a transfer of a malpractice claim and whether the transferee had standing to bring the claim. There was no transfer of a malpractice claim in this case. First, this is not a malpractice claim. Second, there was no transfer since the Respondent still has the breach of fiduciary duty claim.

II.

COLLATERAL ESTOPPEL APPLIES.

Under certain circumstances, a debt is not discharged by a bankruptcy. 11 U.S.C. § 523(a)(4) states that a debt which arises from a "defalcation while acting in a fiduciary capacity" is a non-dischargeable debt. The Bankruptcy Court correctly held that the findings of the State Court that the Petitioner breached his fiduciary duty to Respondent may be applied to this case by collateral estoppel for a finding that the debt is non-dischargeable as a defalcation by a fiduciary. *Johnson v. Miera* (*In re Miera*), 104 B.R. 150, 156 (Bankr. D. Minn. 1989), *affirmed*, 926 F.2d 741 (8th Cir. 1991). In this case there is no question that breach of fiduciary duty was determined in the prior action, was actually litigated, was determined by a valid and final judgment and was essential to that final judgment. Thus, collateral estoppel applies. (There is no longer any question that a state court action can have a collateral estoppel effect in a non-dischargeability action. *See Grogan v. Garner*, 498 U.S. 279, 111 S. Ct. 654, 112 L. Ed. 2d 755 (1991).)

When the Petitioner attacks the findings of the State Court action, he is trying to relitigate issues he has already lost. These findings, no matter how much the Petitioner disagrees with them, cannot be challenged. The Petitioner's attack on the Bankruptcy Court's findings in his brief is irrelevant. Further, the contents of Appendix E of his Appendix is irrelevant as an attack on the State Court Judgment.

The Petitioner further argues that the issue of whether the judgment in the State District Court Judgment was obtained by fraud was not "actually litigated," one of the requirements for collateral estoppel. The Petitioner argued that the dissolution of the Respondent was fraudulently concealed from him

precluding him from raising lack of standing as a defense. (Of course, the Respondent vigorously denies it fraudulently concealed the dissolution.)

This issue was litigated and the State District Court ruled against the Petitioner on this precise point on summary judgment. A trial was not necessary. In other words, the State Court ruled that, as a matter of law, the defense of fraud (for failure to disclose the partnership dissolution) failed. The State District Court had two reasons for granting summary judgment. First, the Petitioner waived this defense. (*See* Petitioner's Appendix at Apdx. 92). The court pointed out that if the dissolution had been disclosed by the Respondent and the Petitioner had raised the issue of standing, the Respondent could have simply filed fees to restore the limited partnership retroactively. (Petitioner's Appendix at Apdx. 97.) Further, its general partner could have restored its corporate status (which had lapsed). (Petitioner's Appendix at Apdx. 97.)

More importantly, the Court cited Ontario law (Ontario Partnership Act, section 38) and found:

> . . . even though Tudor Oaks did not have a right to maintain any action, the only remaining partner, S.B. McLaughlin had a right to continue the action commenced before the partnership dissolved.

(Petitioner's Appendix at Apdx. 98). The court held that even if the Respondent's dissolution was fraudulently concealed, it was irrelevant because S.B. McLaughlin could maintain the case in any event.

The Eighth Circuit agreed that the fraud issue had already been fully litigated and collateral estoppel applied. Therefore, the reason the Petitioner never had a chance to present evidence

in the State Court that the judgment was obtained by fraud was because the defense failed as a matter of law. The Petitioner did actually litigate those issues in the summary judgment proceedings and lost. Accordingly, collateral estoppel applies.

III.

THERE WERE DAMAGES IN THIS CASE.

The Petitioner's first question presented is whether a breach of fiduciary duty resulting in no damage can be a defalcation. However, there were damages caused by the breach of fiduciary duty. The jury found that the breach of fiduciary duty caused damages in the amount of $1,744,568.22 (as later amended). Again, the Petitioner may disagree that the breach of fiduciary duty caused this damage, but collateral estoppel bars him from questioning it. The breach of fiduciary duty did cause damage.

IV.

A DEFALCATION BY A FIDUCIARY DID OCCUR.

The Petitioner argues that no defalcation occurred. It is well established that fiduciary duties that arise constructively are not the type of fiduciary duty required under 11 U.S.C. § 523(a)(4). The Petitioner and Respondent have never disagreed on this point. The Bankruptcy Court and the Eighth Circuit Court of Appeals also reaffirmed this point. *See Davis v. Aetna Acceptance Co.*, 293 U.S. 328, 55 S. Ct. 151, 79 L. Ed. 393 (1934), the cases cited by the Petitioner at page 13-14 of the Petitioner's brief, and the cases in the Bankruptcy Court Order in the Petitioner's Appendix at Apdx. 29. An attorney-client relationship is probably one of the oldest and most recognized forms of fiduciary relationships and does not arise constructively since it exists prior to the "bad acts." Courts have consistently determined that this is the type of fiduciary relationship

recognized by 11 U.S.C. § 523(a)(4) for non-dischargeable purposes. *See In re Marchiando*, 13 F.3d 1111, 1115 (7th Cir. 1994), *cert. denied*, 512 U.S. 1205, 114 S. Ct. 2675, 129 L. Ed 2d 810 (1994) ("So a lawyer is deemed the fiduciary of his client, even if he does not manage a fund entrusted by the client. . . .") These cases hold that the attorney-client fiduciary relationship if breached, can lead to a non-dischargeable debt. *See Kartchner v. Kudla* (*In re Kudla*), 105 B.R. 985 (Bankr. D. Colo. 1989); *Federal Savings and Loan Insurance Corporation v. Mmahat* (*In re Mmahat*), 97 B.R. 293 (E.D. La. 1988), *affirmed in part and remanded*, 907 F.2d 546 (5th Cir. 1990), *cert. denied*, 499 U.S. 936, 111 S. Ct. 1387, 113 L. Ed. 2d 444 (1991) (an unrelated part of this holding involving banking law has been overruled); *Morales v. Codias* (*In re Codias*), 78 B.R. 344 (Bankr. S.D. Fla. 1987); *Schwalbe v. Gans* (*In re Gans*), 75 B.R. 474 (Bankr. S.D.N.Y. 1987); *Douchette v. Kwait* (*In re Kwait*); 62 B.R. 818 (Bankr. D. Mass. 1986), *affirmed in part and vacated in part*, 81 B.R. 184 (D. Mass. 1987); *Purcell v. Janikowski* (*In re Janikowski*), 60 B.R. 784 (Bankr. N.D. Ill. 1986); and *Brawer v. Gelman* (*In re Gelman*), 47 B.R. 735 (Bankr. S.D. Fla. 1985).

The Eighth Circuit Court of Appeals held that the breach of this fiduciary duty was a "defalcation" under 11 U.S.C. § 523(a)(4) and led to the damages. Defalcation is broadly defined and includes the taking of an opportunity that results in the damages to the party from whom it was taken. *See* Bankruptcy Court Order at Apdx. 35, *Pan-Western Life Insurance v. Galbreath* (*In re Galbreath*), 112 B.R. 892 (Bankr. S.D. Ohio 1990); *F.D.I.C. v. Sax* (*In re Sax*), *F.D.I.C. v. Sweeney* (*In re Sweeney*), 106 B.R. 534 (Bankr. N.D. Ill. 1989). For example, an attorney who arranged for improper loans from a bank was guilty of a defalcation. As stated in *F.D.I.C. v. Mmahat*, *supra*, 907 F.2d at 550,

> FDIC argues that there was defalcation: Mmahat . . . [the attorney] . . . urged Gulf Federal to make

> improper loans so that he could earn fees. Mmahat thereby enriched himself at the cost of Gulf Federal's assets. . . . We agree.

See also In re Moreno, 892 F.2d 417 (5th Cir. 1990) (corporate loans arranged for officer's benefit is defalcation). As in *Mmahat*, the Petitioner enriched himself at the expense of the Respondent. As stated by the Bankruptcy Court on Apdx. 37-38 of Petitioner's Appendix,

> It is clear that the Minnesota State Court's unadorned finding the Defendant had breached his fiduciary duty to the Plaintiff in three separate instances is sufficient to make out a "defalcation" within the contemplation of § 523(a)(4).

There is no support of any kind for the Petitioner's position that some type of "bad intent" must exist for a finding of defalcation. (In fact, he cites no support.) To the contrary, all courts have rejected the Petitioner's position. (*See* Bankruptcy Court Order, Petitioner's Appendix at Apdx. 36.) *See also Lewis v. Scott*, 97 F.3d 1182 (9th Cir. 1996).

The Petitioner argues that a defalcation requires a violation of an express trust "res" and that there is none in this case. He cites a Sixth Circuit decision, *Garver v. R.E. America, Inc.*, 116 F.3d 176 (6th Cir. 1997) which states that the fiduciary must actually take property from a trust "res" to commit a defalcation. The statements in that case could result in a definition of defalcation which is more narrow than the definition other courts have used. These cases, exemplified by the Bankruptcy Court order in this case, hold that a formal trust is not necessary. However, the debt must be an obligation which arises from a breach of the fiduciary duty and not other types of obligations. *See F.D.I.C. v. Mmahat*, 907 F.2d 546, 549-550 (5th Cir. 1990), *cert.*

denied, 499 U.S. 936 (1991) (attorney breached duty by advising bank to make bad loans from which he profited); *In re Janikowski*, 60 B.R. 784, 790 (Bankr. N.D. Ill. 1986) (attorney's failure to record deed is a breach of duty); *Pan Western Life Insurance v. Galbreath* (*In re Galbreath*), 112 B.R. 892 (Bankr. S.D. Ohio 1990) (corporate officer breached fiduciary duty by arranging improper loans); and *F.D.I.C. v. Sax* (*In re Sax*), *F.D.I.C. v. Sweeney* (*In re Sweeney*), 106 B.R. 534 (Bankr. D. Ill. 1989) (corporate officer breached duty by arranging for improper loans).

This view is also consistent with the statute, 11 U.S.C. § 523(a)(4), which does not discuss a trust or a trust "res"; it simply provides a debt resulting from defalcation while acting in a fiduciary capacity is not dischargeable. However, these cases, the Bankruptcy Court decision, and the Eighth Circuit decision do not hold that any debt owed by an attorney is not dischargeable, as the Petitioner claims. As pointed out by the Bankruptcy Court and by the opinion cited by the Petitioner, *Fowler Brothers v. Young* (*In re Young*), 91 F.3d 1367, 1372 (10th Cir. 1986), there must be a breach of a "trust relationship" between an attorney and a client to find a defalcation while acting in a fiduciary capacity. In this case, there is no question there was a breach of the trust relationship. This was not a simple debtor/creditor relationship as in *In re Young*, *supra* (a loan) because the breach resulted directly from the fiduciary relationship an attorney has to the client. First, there was a breach of fiduciary duty for taking the twenty percent (20%) interest in the property as a fee for finding purchasers. Second, there was a fiduciary duty breach for purchasing an undisclosed fifteen percent (15%) interest in the property through the Petitioner's investment in KSCS. And, third, there was a breach of fiduciary duty by permitting KSCS shareholders to take the twenty percent (20%) interest expected to go to the Respondent.

The Sixth Circuit's narrow definition is irrelevant to its holding since the *Garver* case did not involve a breach of the

trust relationship; it involved a mere creditor/debtor relationship, which is dischargeable under any test or definition of defalcation. The attorney in that case had breached a promise to invest funds and committed malpractice. Thus, *Garver* would be decided the same way under the test used by the Eighth Circuit and other courts because the debt did not result from a breach of the trust relationship.

In any event, even if the *Garver* statements were used as the defalcation definition, there was a "res" in this case because the opportunity to invest was held in trust by the Petitioner who misused it. The taking of the opportunity was no different from taking money out of a trust account. This case would have the same result in the Sixth Circuit. There is no split between the circuits on the issue of what constitutes a defalcation which must be resolved by this Court to decide this case.

CONCLUSION

For the reasons stated above, the Petitioner respectfully requests that the Court deny the petition.

Respectfully submitted,

WILLIAM J. FISHER
Counsel of Record
GRAY, PLANT, MOOTY,
MOOTY & BENNETT, P.A.
Attorneys for Respondent
Tudor Oaks Limited Partnership
by its Liquidating Trustee,
S.B. McLaughlin & Co.
3400 Multifoods Tower
33 South Sixth Street
Minneapolis, Minnesota 55402
(612) 343-2800

APPENDIX

APPENDIX A — SPECIAL VERDICT FORM

STATE OF MINNESOTA DISTRICT COURT
COUNTY OF HENNEPIN FOURTH JUDICIAL DISTRICT

File No. 87-11035

S.B. McLaughlin & Company, Ltd., Tudor Oaks Condominium Project, an Ontario Limited Partnership; ABIO Holdings (Minnesota) Inc., a Minnesota corporation

Plaintiffs,

vs.

John Cochrane, an individual, and KSCS Properties, Inc., a Minnesota corporation

Defendants.

SPECIAL VERDICT FORM

1. Did Mr. Cochrane breach a fiduciary duty to Tudor Oaks Condominium Project, an Ontario Limited Partnership with respect to the 20% fee charged for legal services? Yes X.

2. If you have answered question no. 1 "Yes," then answer this question: Was such breach a direct cause of damage to Tudor Oaks Condominium Project, an Ontario Limited Partnership? Yes X.

3. Did Mr. Cochrane breach a fiduciary duty to Tudor Oaks Condominium Project, an Ontario Limited Partnership with respect to the relinquishment on December 16, 1966 of the 20% "carried interest"?. Yes X.

Appendix A

4. If you have answered Question no. 3 "Yes," then answer this question: Was said breach a direct cause of damage to Tudor Oaks Condominium Project, an Ontario Limited Partnership? Yes X.

5. Did Mr. Cochrane breach a fiduciary duty to Tudor Oaks Condominium Project, an Ontario Limited Partnership by his purchase personally of fifteen (15%) percent interest in the Sheriff's Certificate of Sale? Yes X.

6. If you have answered Question no. 5 "Yes," then answer this question: Was such breach a direct cause of damage to Tudor Oaks Condominium Project, an Ontario Limited Partnership? Yes X.

7. If you have answered Questions nos. 2, 4, and/or 6 "Yes", then answer this question: What sum of money will fairly and adequately compensate Tudor Oaks Condominium Project, an Ontario Limited Partnership for any loss it sustained as a result of said breach or breaches? $1.628 million.

8. Did KSCS, Inc. and John Cochrane conspire to breach Mr. Cochrane's fiduciary duties to Tudor Oaks Condominium Project, an Ontario Limited partnership? Yes X.

9. If you have answered Question no. 8 "Yes," then answer this question: Was said conspiracy a direct cause of damage to Tudor Oaks Condominium project, an Ontario Limited Partnership? Yes X.

10. What sum of money will fairly and adequately compensate Tudor Oaks Condominium Project, an Ontario Limited Partnership for any loss it sustained as a direct result of said conspiracy? $3.52 million.

Appendix A

11. What was the fair market value on December 17, 1986 of 100% of the interest in the Sheriff's Certificate of Sale that was purchased by KSCS? $5.6 million.

12. Did Mr. Cochrane have a fiduciary duty to S.B. McLaughlin & Company, Ltd., by reason of his representation of Tudor Oaks Condominium Project, an Ontario Limited Partnership? Yes X.

13. If you have answered Question no. 12 "Yes," then answer this question: Did Mr. Cochrane breach said fiduciary duty to S.B. McLaughlin & Company, Ltd.? Yes X.

14. If you have answered Question no. 13 "Yes," then answer this question: Was said breach a direct cause of damage to S.B. McLaughlin & Company, Ltd.? Yes X.

15. What sum of money will fairly and adequately compensate S.B. McLaughlin & Company, Ltd. for any loss it sustained as a result of said breach? $792,000.

THE FOREPERSON:

By: s/ illegible

Time: 11:20 am
Date: illegible

* * *

Supreme Court, U.S.
FILED
FEB 10 1998
CLERK

(3)

No. 97-973

In The
Supreme Court of The United States
October Term 1997

JOHN A. COCHRANE,
Petitioner,

v.

TUDOR OAKS LIMITED PARTNERSHIP,
Respondent.

Petition For A Writ Of Certiorari
To The United States Court of
Appeals For The Eighth Circuit

PETITIONER'S REPLY TO BRIEF IN OPPOSITION

John A. Cochrane
Attorney at Law
24 East Fourth Street
St. Paul, MN 55010
(913) 385-1500

Attorney for Petitioner
Counsel of Record

APPELLATE ADVANTAGE
4264 N. OAK TRAFFICWAY◆KANSAS CITY, MO 64116◆816-453-2424

Pursuant to Rule 15 (b) of the Rules of the Supreme Court of the United States the Petitioner makes the following Response to Respondents Brief in Opposition to Petitioner for Certiorari.

Respondent's Statement of the Case is in error as follows:

1. Petitioner was retained by David Owens, Esq., and the fee of $20,000.00 was paid by David Owen, Esq., on behalf of defendants entities in the deficiency action by First Bank. (Apdx. 149)

2. The Sheriffs Certificate was bid in by the first Bank at the Sheriff's Sale on June 12th of 1986 for $5,600,000.00 and offered for sale in November 17, 1986 by letter offer. (Apdx. 145)

3. The Sheriff's Certificate was purchased from the Bank by K.S.C.S. Inc., a Minnesota Corporation on December 17, 1996. Petitioner and three other investors each contributed $300,000.00 to K.S.C.S. Inc. to make the purchase. (Apdx. 117)

4. Petitioner had no "Agreement" of any nature with Tudor Oaks Limited Partnership by or through its Liquidating Trustee S. B. McLaughlin & Co. Ltd. It was the Owen-Crashley interests individually that hoped to retain an interest in the project if possible. (Apdx. 142 - 144)

5. Respondent's action *ab initio* was a derivative

action and the statutory independent committee authorized by the director found the action to be without merit. (Apdx. 108 - 109)

6. Mr. David Owen, Esq., on behalf of himself, Ownix Ltd., and Tudor Oaks Condominium Project; Mr. Crashley, on behalf of himself and Central Precision, Inc., who made up two thirds of the Limited and the General Partnerships [the other being S. B. McLaughlin Co., Ltd.] testified at trial that they were completely satisfied with petitioners representation.

7. The Court of Appeals reduced the verdict by recalculation of the damages to Tudor Oaks and vacated the verdict as to S. B. McLaughlin Co., Ltd. holding that McLaughlin had no cause of action. (Apdx. 105 - 108)

February 9, 1998

Respectfully Submitted,

John A. Cochrane
Debtor
MN ATTY. I.D. No. 17577
Admitted to Sup. Court
Bar on October 1, 1963.
24 East 4th St.
St. Paul, MN 55101
(612) 298-1950
Fax (612) 298-0089

Of Counsel:
Loper & Seymour, P. A.
Stewart C. Loper
MN ATTY. I.D. No. 64476
24 East 4th St.
Suite 201
St. Paul, MN 55101
(612) 291-2954